Q. II-D-1 Provide a schedule showing all revenues and expenses for the test year and for the 12-month period immediately prior to the test year, together with an explanation for major variances between test year revenues and expenses and those for the previous 12-month period. Revenues and expenses shall be summarized by the major account categories listed below. If budgeted data for a future test year is not readily available by these categories, an analysis of the data for the 12-month period immediately prior to the future test year or for the most recent available calendar year may serve as the basis ratably allocating the budgeted data into the account categories as follows: OPERATING REVENUES 400 Electric Revenues: Residential Sales Commercial Sales Industrial Sales Public Street & Highway Lighting Sales Sales for Resale Total Other Electric Revenues Other Electric Revenues: Late Payment Charges Miscellaneous Service Revenues Rent from Electric Property Other Electric Revenues Total Other Electric Revenues Total Operating Revenues OPERATING EXPENSES 401-2 Operation and Maintenance Expenses Power Production Expenses: Fuel Net Interchange Deferred Energy Costs Other Transmission Expenses Distribution Expenses Customer Service & Informational Expense Sales Expenses Administrative and General Expenses Total Operation & Maintenance Expenses 403 Depreciation Expenses Amortization of Net Salvage Nuclear Decommissioning Expense 407 Amortization of Property Losses Taxes Other Than Income Taxes 408 Total Operating Expenses Prior to Federal & State Income Taxes Operating Income Prior to Federal and State Income Taxes FEDERAL AND STATE INCOME TAXES 409 Federal Income Taxes State Income Taxes Deferred Federal Income Taxes Deferred State Income Taxes Investment Tax Credit Adjustments 411 Deferrals Amortization – Credit Other Income Tax Credits & Charges Total Federal and State Income Taxes Operating Income After Federal and State Income Taxes OTHER INCOME AND DEDUCTIONS OTHER INCOME 415-18 Non-utility Operating Income 419 Interest and Dividend Income Allowance for Other Funds Used During Construction 421 Gain on Disposition of Property Other Miscellaneous Non-operating Income Total Other Income OTHER INCOME DEDUCTIONS 421 Loss on Disposition of Property 425 Miscellaneous Amortization 426 Miscellaneous Total Other Income Deductions TAXES APPLICABLE

TO OTHER INCOME AND DEDUCTIONS 408 Taxes Other Than Income Taxes 409 Federal Income Tax State Income Tax Total Taxes Applicable to Other Income and Deductions Income Before Interest Charges INTEREST CHARGES 427 Interest on Long-Term Debt 428 Amortization of Debt Discount and Expense 429 Amortization of Premium on Debt 431 Other Interest Expense 432 Allowance for Borrowed Funds Used During Construction – Credit Net Interest Charges Income Before Extraordinary Items Extraordinary Items After Taxes Net Income

A. II-D-1

Refer to Attachment II-D-1(a), which was prepared by witness Michael J. Trzaska, and Attachment II-D-1(b), which was prepared by witness Robert J. Stefani, for the requested comparison of revenues and expenses between the Company's claims for the fully projected future test year (2022) and the future test year (2021) and amounts recorded on its books of account for the historic test year (2020), as well as explanations of the variances between projected and actual amounts.

PECO Electric Operations
Before The Pennsylvania Public Utility Commission
( $ in Thousands )

Revenue and Expense Comparison for 2020, 2021 and 2022

| Line No. | Category | Description | Account | (1) Pennsylvania Jurisdictional 2020 | (2) Pennsylvania Jurisdictional 2021 | (3) Pennsylvania Jurisdictional 2022 |
|---|---|---|---|---|---|---|
| 1 | **Total Operating Revenues** | Residential | 440.0 | $1,298,478 | $1,256,628 | $1,270,389 |
| 2 | | Residential - House Heating | 440.1 | 262,323 | 278,422 | 280,724 |
| 3 | | C & I Small | 442.0 | 348,181 | 361,253 | 384,582 |
| 4 | | C & I Large | 442.1 | 197,646 | 230,121 | 249,636 |
| 5 | | Street Lighting | 444.0 | 7,581 | 9,722 | 10,471 |
| 6 | | Railroads & Railways | 446.0 | 20,539 | 20,528 | 20,971 |
| 7 | | Intercompany | 448.0 | 896 | 1,243 | 1,283 |
| 8 | | Transmission - All Classes | | 163,241 | 159,275 | 172,082 |
| 9 | | **Total Operating Revenue** | | $2,298,884 | $2,317,192 | $2,390,139 |
| 10 | | | | | | |
| 19 | | Sales For Resale | 447.0 | $96 | | |
| 20 | | Forfeited Discounts | 450.0 | 3,064 | $6,925 | $12,795 |
| 21 | | Miscellaneous Service Revenues | 451.0 | 2,663 | 3,829 | 3,829 |
| 22 | | Rent For Electric Property | 454.0 | 18,662 | 18,716 | 19,219 |
| 23 | | Other Electric Revenues | 456.0 | 14,759 | 12,287 | 12,633 |
| 24 | | Transmission of Electricity for Others | 456.1 | | | |
| 26 | | | | | | |
| 27 | | **Total Revenues** | | $2,338,127 | $2,358,950 | $2,438,616 |
| 28 | | | | | | |
| 29 | **Total Operating Expenses** | Purchased Power | | $681,112 | $680,389 | $689,927 |
| 30 | | Transmission Expenses | | 153,066 | 149,140 | 161,192 |
| 31 | | Distribution Expenses | | 411,617 | 367,735 | 370,979 |
| 32 | | Customer Accounts Expenses | | 107,636 | 116,780 | 119,238 |
| 33 | | Customer Service & Information Expenses | | 75,144 | 77,598 | 102,672 |
| 34 | | Sales Expense | | 667 | 1,602 | 1,676 |
| 35 | | Administrative & General Expense | | 168,611 | 156,346 | 160,384 |
| 36 | | | | | | |
| 37 | | **Total Operating Expenses** | | $1,597,853 | $1,549,591 | $1,606,068 |
| 38 | | | | | | |
| 39 | | Depreciation & Amortization Expense | | $234,870 | $232,930 | $260,755 |
| 40 | | Taxes Other Than Income Taxes | | 161,192 | 159,849 | 163,581 |
| 41 | | | | | | |
| 42 | | **Total Expenses** | | $1,993,915 | $1,942,370 | $2,030,404 |
| 43 | | | | | | |
| 44 | | **Total Operating Income Before Income Taxes** | | $344,212 | $416,580 | $408,211 |
| 45 | | | | | | |
| 46 | | Federal and State Income Taxes | | ($6,572) | $25,274 | $28,122 |
| 47 | | Deferred Income Taxes | | (7,850) | 18,304 | 9,269 |
| 48 | | ITC Amortization | | (23) | (22) | (20) |
| 49 | | **Net Income Tax Expenses** | | ($14,445) | $43,556 | $37,371 |
| 50 | | | | | | |
| 51 | | **Net Operating Income** | | $358,657 | $373,024 | $370,840 |

Total Revenue for 2021 is $21M higher than 2020. The main drivers are:

- DSIC revenue increased by $9M for recovery of LTIIP spending
- Forfeited Discounts Revenues and Reconnect Fees increased by $6M due to the non-collection during the COVID-19 moratorium in 2020
- Weather normalized sales increased by $4M primarily due to COVID-19 impact in 2020
- Make Ready revenue increased by $4M, which is offset in O&M expense
- Decreased operating revenues of ($2M) due to favorable weather in 2020

Total Revenue for 2022 is $80M higher than 2021. The main drivers are:

- DSIC revenue increased by $26M for recovery of LTIIP spending
- Energy Efficiency program cost recovery of $23M, which is offset in O&M expense
- Retail Transmission revenue increased by $13M, which is offset in Transmission Cost
- Energy Revenue increased by $9M primarily driven by higher energy prices, which is offset in Power Supply Cost
- Forfeited Discounts Revenues and Reconnect Fees expected to increase by $6M as COVID-19 moratorium is lifted in 2021 and collections resume

Total Operating Expenses for 2021 are ($48M) lower than 2020. The main drivers are:

- Lower Transmission Cost of ($4M), which is primarily offset in Operating Revenue
- Lower Distribution Expenses of ($44M) primarily caused by the lower major storm reserve total in 2021 compared to 2020, which had two major storm events.
- Higher Customer Accounts Expenses of $9M are primarily driven by lower Customer Operations contracting and overtime in 2020 related to COVID impacts and the extended moratorium.
- Higher Customer Service and Information expenses of $2M are primarily due to an increase in expenditures for Act 129 Energy Efficiency programs.
- Lower Administrative & General Expenses of ($12M) are primarily driven by lower injuries and damages expense in 2021

  PECO does not budget by FERC account.  Please refer the Company's response to SDR-OM-02 for more detailed variance explanations by natural expense codes, which exclude Energy Efficiency costs.

Total Operating Expenses for 2022 are $56M higher than 2021. The main drivers are:

- Higher Power Supply Cost of $10M, which is primarily offset in Operating Revenue
- Higher Transmission Cost $12M, which is primarily offset in Operating Revenue

- Higher Distribution Expenses of $3M are primarily driven by inflationary impacts upon base payroll and contracting, which are offset by reductions in pension and benefit costs.
- Higher Customer Accounts Expense by $2M are primarily driven by inflationary impacts upon base payroll and contracting, which are offset by reductions in bad debt expense and pension and benefit costs.
- Higher Customer Service and Information expenses of $25M are primarily due to an increase in expenditures for Act 129 Energy Efficiency programs.
- Higher Administrative & General Expenses of $4M are primarily driven by inflationary impacts upon base payroll and contracting, which are offset by reductions in pension and benefit costs.

  PECO does not budget by FERC account. Please refer the Company's response to SDR-OM-02 for more detailed variance explanations by natural expense codes, which exclude Energy Efficiency costs.

<u>Total Depreciation and Amortization Expense for 2021 is ($2M) lower than 2020. The main drivers are:</u>

- Higher Plant Depreciation of $11M as a result of increased investment
- Higher Software IT Amortization of $5M as a result of increased investment
- Lower Reg Asset Amortization due to fully Amortized Programs of ($16M)
- Lower Energy Efficiency Program Amortization of ($2M)
- Higher DSP Related IT Costs $1M

<u>Total Depreciation and Amortization Expense for 2022 is $28M higher than 2021. The main drivers are:</u>

- Higher Plant Depreciation of $23M as a result of increased investment
- Higher Software IT Amortization of $6M as a result of increased investment
- Full Amortization of Energy Efficiency Program of ($2M)

<u>Total Taxes Other Than Income for 2021 are ($1M) lower than 2020 due primarily to:</u>

- Lower use tax accrual is due to non-recurring adjustments recorded in 2020.

<u>Total Taxes Other Than Income for 2022 are $4M higher than 2021 due primarily to:</u>

- Higher Gross Receipts Tax related to higher retail revenue of $4M

Total Income Taxes for 2021 are $58M higher than 2020 due primarily to:

- Higher State Income Tax of $8M is primarily driven by higher pre-tax income and property-related timing differences
- Higher Federal Income Tax of $27M is primarily driven by higher pre-tax income, property-related timing differences
- Higher Deferred Income Tax of $23M is primarily driven by property-related timing differences

Total Income Taxes for 2022 are ($6M) lower than 2021 due primarily to:

- Higher State Income Tax of $1M is primarily driven by property-related timing differences partially offset by decrease in pre-tax income
- Higher Federal Income Tax of $2M is primarily driven by property-related timing differences partially offset by decrease in pre-tax income
- Lower Deferred Income Tax of ($9M) is primarily driven by property-related timing differences

Q. II-D-2

Provide a summary of test year adjustments which sets forth the effect of the adjustment upon the following: operating revenues, operating expenses, taxes other than income taxes, operating income before income taxes, State income tax, Federal income tax and income available for return. In addition, test year adjustments shall be presented on the basis of the major account categories set out at II-D-1.

A. II-D-2

Refer to Schedules D-3 and D-5 of Exhibits MJT-1 and MJT-2 for a summary of each proposed adjustment for the fully projected future test year and future test year, respectively. The impact on taxes other than income is reflected on Schedule D-16, and the impact on State and Federal income taxes is shown on Schedule D-18. The referenced schedules are discussed in PECO Statement No. 3, the Direct Testimony of Michael J. Trzaska.

Q. II-D-3

List and explain all nonrecurring or extraordinary expenses incurred in the test year and all expenses included in the test year which do not occur yearly but are of a nature that they do occur over an extended period of years, for example, non-yearly maintenance programs, and the like.

A. II-D-3

The Company incurred extraordinary expenses of $9.9M in the historic test year in relation to the COVID-19 pandemic. These expenses include increases in employee-related costs (including required enhancements to employee sick-leave benefits), for personal protective equipment, and in labor and contracting costs due to the impact on productivity of complying with social distancing and other measures designed to protect employees, customers, and the general public during the COVID-19 pandemic.

The Company has also incurred incremental bad debt expense related to the COVID-19 pandemic totaling $37.9M in 2020 and expects to incur additional incremental bad debt expense in 2021 totaling $10.3M. In accordance with the Secretarial Letter dated May 13, 2020, the Company has created a regulatory asset for these amounts of incremental bad debt expense as shown on PECO Statement No.3, the direct testimony of Michael J. Trzaska, PECO Exhibit MJT-3, Schedule D-11, page 76, column 2, line 7. As a result of creating the regulatory asset, these amounts are not included in operating expense in the historic test year (2020) or future test year (2021). The total bad debt regulatory asset will be amortized over 3 years and is included in Schedule D-11 as a pro-forma adjustment.

Due to the extended termination moratorium effective since mid-March 2020, the Company's accounts receivable balances in 2020 have increased significantly above the normal level and are not expected to return to normal levels until after the FPFTY.  The Company expects to incur incremental carrying costs of $17.3M related to this impact to cash working capital driven by COVID-19.  The total incremental carrying costs will be amortized over 3 years and is included in PECO Exhibit

MJT-3, Schedule D-14, page 79, column 2, line 8 as a pro-forma adjustment.

| | |
|---|---|
| Q. II-D-4 | As a separate item, list extraordinary property losses related to property previously included in cost of service when the gain or loss on this property has occurred or is likely to occur in the future test year. The proposed ratemaking treatment of extraordinary gains and losses must also be disclosed. Sufficient supporting data must be provided. |
| A. II-D-4 | No claim is being made for extraordinary property losses. |

Q. II-D-5 Provide the amount of accumulated reserve for uncollectible accounts, method and rate of accrual, amounts accrued, and amounts written-off in each of last three years.

A. II-D-5

| Uncollectible Accounts *(in thousands)* | | | |
|---|---|---|---|
| **Year** | **Ending Reserve Balance*** | **Write-offs**** | **Change in Reserve** |
| 2018 | $(64,768) | $32,142 | $(33,769) |
| 2019 | (61,485) | 31,350 | (28,068) |
| 2020 | (117,490) | 15,985 | (71,991) |

*Represents reserve for uncollectible customer accounts at the end of each year for electric services only. Does not include reserve for late payment charges.

**The write-offs above includes $5,259, $3,514, and $2,014 of write-offs for the years ended December 31, 2018, 2019, and 2020, respectively, related to the in-program arrearage forgiveness program (Docket No. M-2012-2290911) which have been excluded from Schedule D-10 in Exhibit MJT-1, MJT-2 and MJT-3.

PECO estimates the allowance for credit losses on customer receivables by applying loss rates developed specifically for PECO based on historical loss experience, current conditions, and forward-looking risk factors to the outstanding receivable balance by customer risk segment. Risk segments represent a group of customers with similar forward-looking credit quality indicators and risk factors that are comprised based on various attributes, including delinquency of their balances and payment history and represent expected future customer behavior. Loss rates applied to the accounts receivable balances are based on a historical average of charge-offs as a percentage of accounts receivable in each risk segment. PECO's customer accounts are generally considered delinquent if the amount billed is not received by the time the next bill is issued, which normally occurs on a monthly basis. PECO's customer accounts are written off consistent with approved regulatory requirements.

Q. II-D-6 Supply detailed calculations to support the total claim for rate case expense, including supporting data for outside service rendered. Provide the items comprising the estimated rate case expense claim for the current rate case.

A. II-D-6 Refer to Schedule D-7 of Exhibits MJT-1, MJT-2, MJT-3 and PECO Statement No. 3, the direct testimony of Michael J. Trzaska.

Q. II-D-7

Submit schedules for the test year and for the 12-month period immediately prior to the test year showing by major components, if included in claimed test year expenses, the expenses incurred in each of the following expense categories.

a. Miscellaneous general expenses, including account 930.

b. Outside service expenses.

c. Regulatory commission expenses.

d. Advertising expenses, including advertising engaged in by trade associations whenever the utility has claimed a contribution to the trade association as a ratemaking claim – provide explanation of types and purposes of such advertising.

e. Research and development expenses – provide a listing of major projects.

f. Charitable and civic contributions, by recipient and amount.

A. II-D-7

a. Refer to Attachment II-D-7(a) for Miscellaneous general expenses, including account 930 for distribution.

b. Refer to Attachment II-D-7(a) for Outside service expenses for distribution. Also refer to Attachment SDR-OM-16(a) for detailed breakdown for Outside service expenses for the HTY.

c. Refer to Attachment II-D-7(a) for Regulatory commission expenses for distribution.

d. Refer to Attachment II-D-7(a) for Advertising expenses for distribution.

e. Refer to Attachment II-D-7(a) for a listing of major projects for Research and Development expenses for distribution.

f. Charitable and civic contributions are not included in the Company's test year claim.

**PECO Energy Company**

**Regulatory Commission, Miscellaneous General, Outside Services Employed, Advertising, and Research and Development Expenses for Electric Distribution**
**Years Ended December 31,**
***(Thousands of Dollars)***

| Line No. | Expense | 2020 | | 2021 | | 2022 | |
|---|---|---|---|---|---|---|---|
| | **Account 930.2 Miscellaneous General Expenses** | | | | | | |
| 1 | Industry Association Dues | $ 564 | | $ 610 | | $ 555 | |
| 2 | Other Experimental and General Research Expenses | 48 | | $ 52 | | $ 47 | |
| 3 | Bank and Other Fees Related to Credit Facilities | 693 | | $ 749 | | $ 683 | |
| 4 | Environmental Remediation Expenses and Reserve Adjustments | 11 | | $ 12 | | $ 11 | |
| 5 | Corporate Dues | 172 | | $ 186 | | $ 169 | |
| 6 | Board of Director Fees | 245 | | $ 265 | | $ 242 | |
| 7 | Surety Bond Expense | 59 | | $ 63 | | $ 58 | |
| 8 | R&D Membership Fees | 343 | | $ 370 | | $ 338 | |
| 9 | Miscellaneous Adjustments | 30 | | $ 32 | | $ 29 | |
| 10 | Total Account 930.2 | $ 2,164 | | $ 2,340 | (a) | $ 2,132 | (a) |

**Notes:**

(a) PECO does not budget at the FERC account level. Category lines reflect budgeted amounts where possible.

| Line No. | Expense | 2020 | | 2021 | | 2022 | |
|---|---|---|---|---|---|---|---|
| | **Account 923 - Outside Services Employed** | | | | | | |
| 11 | BSC - Various | $ 59,072 | (1) | | | | |
| 12 | Contracting Services | 6,240 | | | | | |
| 13 | Contracting Professional | 3,537 | | | | | |
| 14 | Total Account 923 | $ 68,850 | | $ 72,315 | (a) | $ 73,413 | (a) |

**Notes:**

(1) Relates to Exelon Business Service Company, LLC (BSC) that provides a variety of corporate support services to PECO Energy Company (PECO). The core shared services BSC provides include Information Technology, Supply, Legal Services, Human Resources, Transportation, and Real Estate. BSC also provides corporate governance services, which include areas such as Finance, Corporate Development, Government and Regulatory Affairs, Corporate Communications and Executive Services.

(a) PECO does not budget at the FERC account level. Category lines reflect budgeted amounts where possible.

**PECO Energy Company**

**Regulatory Commission, Miscellaneous General, Outside Services Employed, Advertising, and Research and Development Expenses for Electric Distribution**
**Years Ended December 31,**
***(Thousands of Dollars)***

| Line No. | Expense | 2020 | | 2021 | | 2022 | |
|---|---|---|---|---|---|---|---|
| | **Account 928.0 - Regulatory Commission Expenses** | | | | | | |
| 15 | Pennsylvania Public Utility Commission General Assessment | $ 6,630 | | | | | |
| 16 | Pennsylvania Office of Consumer Advocate General Assessment | 642 | | | | | |
| 17 | Pennsylvania Office of Small Business Advocate General Assessment | 163 | | | | | |
| 18 | Pennsylvania Damage Prevention Committee General Assessment | 14 | | | | | |
| 19 | Pennsylvania Public Utility Comission Electric Distribution Rate Case | 492 | | | | | |
| 20 | Total Account 928 | $ 7,941 | | $ 7,439 | (a) | $ 7,582 | (a) |

**Notes:**

(a) PECO does not budget at the FERC account level. Category lines reflect budgeted amounts where possible.

| Line No. | Expense | 2020 | | 2021 | | 2022 | |
|---|---|---|---|---|---|---|---|
| | **Account(s) 909.0, 930.1, 913.0 - Advertising Expenses (2)** | | | | | | |
| 21 | Customer Education | $ 448 | | | | | |
| 22 | Customer Assistance Programs | 313 | | | | | |
| 23 | Miscellaneous | 281 | | | | | |
| 24 | Total Accounts (Advertising Expenses) | $ 1,042 | | $ 1,329 | (a) | $ 1,351 | (a) |

**Notes:**

(2) Account 930.1 does have activity posted during 2020; however, based on the recipients of the payments (expense) booked to account 930.1, the activity is deemed to be non-recoverable and is not included on this schedule in response to this request.

(a) PECO does not budget at the FERC account level. Category lines reflect budgeted amounts where possible.

| Line No. | Expense | 2020 | | 2021 | | 2022 | |
|---|---|---|---|---|---|---|---|
| | **Research and Development Expenses** | | | | | | |
| 25 | Electric Power Research Institute (EPRI) | $ 297 | | $ 322 | | $ 293 | |
| 26 | Georgia Tech Research Corp | 20 | | $ 22 | | $ 20 | |
| 27 | Centre for Energy Advancement through Technological Innovation | 13 | | $ 14 | | $ 12 | |
| 28 | Watson & Renner | 7 | | $ 8 | | $ 7 | |
| 29 | Arizona State University | 4 | | $ 5 | | $ 4 | |
| 30 | University of Colorado Foundation | 1 | | $ 1 | | $ 1 | |
| 31 | Other | 48 | | $ 52 | | $ 47 | |
| 32 | Total Research and Development Expenditures | $ 391 | (3) | $ 422 | (3), (a) | $ 385 | (3), (a) |

**Notes:**

**PECO Energy Company**

**Regulatory Commission, Miscellaneous General, Outside Services Employed, Advertising, and Research and Development Expenses for Electric Distribution**
**Years Ended December 31,**
***(Thousands of Dollars)***

| Line No. | Expense | 2020 | 2021 | 2022 |
|---|---|---|---|---|

(3) included in account 930.2; refer to line item(s) 2 and 8 of section above.
(a) PECO does not budget at the FERC account level. Category lines reflect budgeted amounts where possible.

**Charitable Contributions**

Note: These expenses are classified as "below the line" and are not included for rate-making purposes.
Accordingly, these expenses are not included on this schedule in response to this request.

Q. II-D-8

Provide an analysis by function of charges by affiliates, for the test year and the 12-month period immediately prior to the test year, for services rendered included in the operating expenses of the filing company. Explain the nature of the service and the basis on which charges or allocations are made, including a copy of an applicable contract. Also, explain major variances between the charges for the test year and the correspondence charges for the prior 12-month period.

A. II-D-8

Refer to Attachment II-D-8(a) for 2020 actual and budgeted 2021 and 2022 expenditures for services rendered by Exelon Business Services Company (BSC) and other affiliate services.

Refer to Company's response to SDR-OM-15, as well as attachments therein of all contracts and service catalogs between the Company and its parent or an affiliated company, for the nature of the services and the basis on which charges or allocations are made.

**PECO Energy Co.**
EBSC and Other Affiliates Operations & Maintenance Costs
**Presentation Basis: PECO Electric Distribution**



($ in thousands)

| Ln. Ref. | | 2020 Actual | 2021 Budget | 2022 Budget |
|---|---|---|---|---|
| 1 | **Charges billed by EBSC** | | | |
| 2 | **Non-Information Technology (IT) Costs:** | | | |
| 3 | Communication | 1,659 | 1,481 | 1,658 |
| 4 | Executives | 7,830 | 4,630 | 4,452 |
| 5 | Exelon Utilities | 4,314 | 7,866 | 7,384 |
| 6 | Finance | 12,156 | 12,658 | 13,508 |
| 7 | Government Affairs | 1,398 | 1,367 | 1,510 |
| 8 | Human Resource | 5,336 | 5,613 | 5,712 |
| 9 | Legal Governance | 5,470 | 6,561 | 6,161 |
| 10 | Security | 5,395 | 5,477 | 5,523 |
| 11 | Supply | 667 | 697 | 710 |
| 12 | Other EBSC Services | 639 | 611 | 455 |
| 13 | **Total Non-IT:** | **44,865** | **46,961** | **47,072** |
| 14 | | | | |
| 15 | **IT Costs:** | | | |
| 16 | EBSC IT | 66,916 | 66,368 | 67,866 |
| 17 | **Total IT Costs:** | **66,916** | **66,368** | **67,866** |
| 18 | | | | |
| 19 | **Total IT and Non-IT Costs:** | **111,781** | **113,330** | **114,938** |
| 20 | | | | |
| 21 | **Total Charges billed by EBSC (excluding Non-Utility):** | **110,341** | **112,586** | **114,077** |
| 22 | | | | |
| 23 | **Non-Utility Charges:** | | | |
| 24 | Charitable Contributions | 506 | 566 | 667 |
| 25 | Lobbying / Other | 933 | 177 | 194 |
| 26 | **Total Non-Utility Charges:** | **1,440** | **744** | **861** |
| 27 | | | | |
| 28 | **Total EBSC Charges (including Non-Utility):** | **111,781** | **113,330** | **114,938** |
| 29 | | | | |
| 30 | **Other Affiliate Charges (Not Above)** | | | |
| 31 | Calibration Testing from Exelon Power Labs | 722 | 591 | 603 |
| 32 | Information Technology from ComEd | 329 | - | - |
| 33 | Information Technology from BGE | 293 | - | - |
| 36 | Information Technology from PHISCO | 18 | - | - |
| 32 | Mutual Assistance ComEd | 9,728 | - | - |
| 33 | Mutual Assistance DPL | 489 | - | - |
| 36 | Mutual Assistance BGE | 263 | - | - |
| 32 | Mutual Assistance PHISCO | 11 | - | - |
| 33 | Inspection Services Clearsight | 93 | - | - |
| 33 | Materials ACE | 2 | - | - |
| 37 | **Total Other Affiliate Charges:** | **11,948** | **591** | **603** |
| 38 | | | | |
| 39 | **Total EBSC and Other Affiliate Charges:** | **123,729** | **113,921** | **115,541** |

| | |
|---|---|
| Q. II-D-9 | Prepare a detailed schedule for the test year showing types of social and service organization memberships paid for, the cost thereof, the accounting treatment and whether included in claimed test year expenses. |
| A. II-D-9 | No social and service organization memberships are included in the Company's claimed test year expenses. |

Q. II-D-10

Provide the following payroll and employee benefit data – regular and overtime – separately for the test year and for the 12-month period immediately prior to the test year:

a. The average and year-end number of employees and the unadjusted annual payroll expenses and employees benefit expense associated with union personnel.

b. The average and year-end number of employees and the unadjusted annual payroll expense and employee benefit expense associated with nonunion personnel.

c. The average and year-end number of employees and the unadjusted annual payroll expense and employee benefit expense associated with management employees, if different than b.

d. A summary of the wage rate, salary and employee benefit changes granted or to be granted during the year.

e. The claimed test year payroll expense and employee benefit expense.

f. The percentage of payroll expense and employee benefit expense applicable to operation and maintenances and the basis thereof.

A. II-D-10

Refer to Attachment II-D-10(a).

**a. Average and year end number of union employees:** (1)

| | Average | Year End |
|---|---|---|
| 2019 | 986 | 992 |
| 2020 | 977 | 960 |
| 2021 | 994 | 1,020 |

**b. Average and year end number of non-union employees:** (1)

| | Average | Year End |
|---|---|---|
| 2019 | 970 | 998 |
| 2020 | 1,017 | 1,054 |
| 2021 | 1,108 | 1,136 |

**c. Average and year end number of exempt management and professional employees:** (1)

| | Average | Year End |
|---|---|---|
| 2019 | 782 | 809 |
| 2020 | 823 | 853 |
| 2021 | 900 | 923 |

(1) Payroll and Benefit expenses are not available by union/non-union and management/professional splits

**d. The average wage increases for hourly employees (1/1) and salaried employees (3/1) are listed below:**

| | 2020 Actual | 2021 Budget |
|---|---|---|
| 1/1 Employees | 2.5% | 2.5% |
| 3/1 Employees | 2.5% | 2.5% |

All job title salaries are based on market reference range. The movement of the range impacts the employee's year end merit increase based on the location in the range.

Contract negotiations are in progress for hourly union employees and should be finalized in March of 2021.

**e. Distribution O&M payroll and benefits expenses are as follows:**

| | 2019 $M | 2020 $M | 2021 Budget $M | 2022 Budget $M |
|---|---|---|---|---|
| Distribution Payroll | 117 | 116 | 123 | 139 |
| Distribution OT | 35 | 44 | 23 | 23 |
| Distribution P&B | 25 | 23 | 22 | 20 |

Note: Results are GAAP based to align budget values

**f. The percentage of payroll expense and employee benefit expense applicable to O&M are as follows:**

| | 2019 | 2020 | 2021 Budget | 2022 Budget |
|---|---|---|---|---|
| Distribution Payroll | 60% | 59% | 55% | 57% |
| Distribution OT | 56% | 57% | 59% | 58% |
| Distribution P&B | 59% | 59% | 55% | 53% |

<u>Basis of O&M</u>

Payroll: Direct labor is budgeted to projects with an O&M and capital split. Back office and other support labor is allocated based on the direct labor and contracting splits

OT: Budgeted to categories of work with O&M and capital splits. Categories of work are based on historical data.

P&B: Generally allocated to O&M and capital based on payroll split to O&M and capital

Q. II-D-11 Describe costs relative to leasing equipment, including computer rentals, and office space, including terms and conditions of the leases. State method for calculating monthly or annual payments.

A. II-D-11 Refer to Attachment II-D-11(a).

**PECO Energy Company**
**Lease Costs Allocated to Electric Distribution**

| Type of Lease | Payment Amount | Frequency | | Length of Lease | | Lease Commencement Date |
|---|---|---|---|---|---|---|
| Copier | $ 53,089 | Monthly | A | Various | B | Various |
| Land | $ 27,271 | Annual | | Various | B | Various |
| Office Building | $ 4,755 | Monthly | A | Five years beginning on January 1, 2017 and terminating December 31, 2021 | | Amended 10/11/2016 |

A - The payment amount was calculated using the average expense attributable to Electric distribution for the year-ended December 31, 2020.
B - Length of lease and commencement date varies based on individual leases.

Q. II-D-12

Submit a statement of past and anticipated changes, since the previous rate case, in major accounting procedures, explain any differences between the basis or procedure used in allocations of revenues, expenses, depreciation and taxes in the current rate case and that used in the prior rate cases, and list all internal and independent audit reports for the most recent 2 year period.

A. II-D-12

Refer to Attachment II-D-12(a). As PECO filed an electric base rate case in 2018, the requested information on significant accounting policies is found in FERC Form 1, Footnote 1 – Significant Accounting Policies and in the SEC Form 10-K for 2018, 2019, 2020. See the Company's response to SDR-GEN-02 for the 2020 FERC form. As the information in those two reports each year are identical, only the relevant pages from the FERC Form 1 are attached.

Refer to Attachment II-D-12(b) for a list of internal audit reports issued in 2019 and 2020.

Refer to Attachment II-D-12(c) for the external audit reports. The external audit reports are Management's Report on Internal Control Over Financial Reporting dated February 11, 2020 and February 24, 2021 and the Report of Independent Registered Public Accounting Firm dated February 11, 2020 and February 24, 2021.

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**PECO Energy Company**
**Condensed Notes to Financial Statements**
**(Dollars in millions, unless otherwise noted)**

## 1. Significant Accounting Policies

### Description of Business

Incorporated in Pennsylvania in 1929, PECO Energy Company (PECO) is engaged principally in the purchase and regulated retail sale of electricity and the provision of transmission and distribution services to residential, commercial and industrial customers in southeastern Pennsylvania, including the City of Philadelphia, as well as the purchase and regulated retail sale of natural gas and the provision of distribution services to residential, commercial and industrial customers in the Pennsylvania counties surrounding the City of Philadelphia. PECO is subject to extensive regulation by the Pennsylvania Public Utility Commission (PAPUC) as to electric and gas distribution rates and service, the issuances of certain securities and certain other aspects of PECO's operations. PECO is a public utility under the Federal Power Act subject to regulation by the Federal Energy Regulatory Commission (FERC) as to transmission rates and certain other aspects of PECO's business and by the U.S. Department of Transportation as to pipeline safety and other aspects of gas operations. Additionally, PECO is also subject to the North American Electric Reliability Corporation (NERC) mandatory reliability standards. Pursuant to the Pennsylvania Electricity Generation Customer Choice and Competition Act of 1996 (Competition Act), the Commonwealth of Pennsylvania required the unbundling of retail electric services in Pennsylvania into separate energy transmission and distribution services with open retail competition for generation services. PECO serves as the local distribution company providing electric distribution services in its franchised service territory in southeastern Pennsylvania and energy service to customers who do not choose a competitive electric generation supplier or who choose to return to the utility after taking service from a competitive electric generation supplier.

### Basis of Presentation

PECO is a principal indirect subsidiary of Exelon Corporation (Exelon), which indirectly owns 100% of PECO's common stock. At December 31, 2017 and 2016, PECO's common stock without par value consisted of 500,000,000 shares authorized and 170,478,507 shares outstanding.

Accounting policies for regulated operations are in accordance with those prescribed by the regulatory authorities having jurisdiction, principally the PAPUC and FERC. The accompanying financial statements have been prepared in accordance with the accounting requirements of FERC as set forth in the Uniform System of Accounts (USOA) and accounting releases, which differ from accounting principles generally accepted in the United States of America (GAAP). The principal differences from GAAP include the exclusions of current maturities of long-term debt from current liabilities, the exclusion of debt issuance costs from long-term debt, the requirement to report deferred tax assets and liabilities separately rather than as a single amount, the classification of accrued taxes as assets and liabilities rather than a net amount, the exclusion of FIN 48 liabilities related to temporary income tax differences, and the classification of certain other assets and liabilities as current instead of noncurrent.

PECO's investments in its subsidiaries, ExTel Corporation, LLC, PECO Wireless, LLC, PECO Energy Capital Trust IV (PECO Trust IV) and PECO Energy Capital Corporation (PECC) are accounted for under the equity method of

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accounting in accordance with the USOA. PECO Wireless, LLC is the parent company of ATNP Finance Company and sole member of PEC Financial Services, LLC. PECC is the general partner of PECO Energy Capital, L.P., which is the grantor of PECO Energy Capital Trust III (PECO Trust III). ExTel Corporation, LLC and PECO Wireless, LLC are consolidated in PECO's GAAP Financial Statements.

**Use of Estimates**

The preparation of financial statements in conformity with USOA and GAAP requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Areas in which significant estimates have been made include, but are not limited to, the accounting for asset retirement obligations (AROs), pension and other postretirement benefits, inventory reserves, allowance for uncollectible accounts, asset impairments, derivative instruments, fixed asset depreciation, environmental remediation costs, taxes and unbilled energy revenues. Actual results could differ from those estimates.

**Accounting for the Effects of Regulation**

PECO applies the authoritative guidance for accounting for certain types of regulation, which requires PECO to record in its financial statements the effects of cost-based rate regulation for entities with regulated operations that meet the following criteria: (1) rates are established or approved by a third-party regulator; (2) rates are designed to recover the entity's cost of providing services or products; and (3) there is a reasonable expectation that rates designed to recover costs can be charged to and collected from customers. PECO accounts for its regulated operations in accordance with regulatory and legislative guidance from the regulatory authorities having jurisdiction, principally PAPUC under state public utility laws and the FERC under various Federal laws. Regulatory assets and liabilities are amortized and the related expense or revenue is recognized in the Statement of Income consistent with the recovery or refund included in customer rates. PECO believes that it is probable that its currently recorded regulatory assets and liabilities will be recovered and settled, respectively, in future rates. However, PECO continues to evaluate its ability to continue to apply the authoritative guidance for accounting for certain types of regulation, including consideration of current events in its regulatory and political environments. If a separable portion of PECO's business was no longer able to meet the criteria discussed above, PECO would be required to eliminate from its financial statements the effects of regulation for that portion, which could have a material impact on its results of operations and financial position. See Note 2—Regulatory Matters for additional information.

With the exception of income tax-related regulatory assets and liabilities, PECO classifies regulatory assets and liabilities with a recovery or settlement period greater than one year as both current and non-current in its Balance Sheet, with the current portion representing the amount expected to be recovered from or settled to customers over the next twelve-month period as of the balance sheet date. Income tax-related regulatory assets and liabilities are classified entirely as non-current on PECOs' Balance Sheets to align with the classification of the related deferred income tax balances.

PECO treats the impacts of a final rate order received after the balance sheet date but prior to the issuance of the financial statements as a non-recognized subsequent event, as the receipt of a final rater order is a separate and distinct event that has future impacts on the parties affected by the order.

**Revenues**

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**Operating Revenues.** Operating revenues are recorded as service is rendered or energy is delivered to customers. At the end of each month, PECO accrues an estimate for the unbilled amount of energy delivered or services provided to customers. PECO records its best estimate of its transmission revenue impacts resulting from changes in rates that PECO believes is probable of approval by FERC in accordance with its formula rate mechanisms. See Note 3—Accounts Receivable for further information.

**Income Taxes**

Deferred Federal and state income taxes are recorded on significant temporary differences between the book and tax basis of assets and liabilities and for tax benefits carried forward. Investment tax credits have been deferred on PECO's Balance Sheet and are recognized in book income over the life of the related property. In accordance with USOA, PECO reports deferred income tax balances arising from temporary differences in Accounts 190, 282 and 283 as appropriate, which differs from the net presentation required by GAAP. See Note 9 - Income Taxes for additional information. PECO recognizes accrued interest related to unrecognized tax benefits in Interest expense or Interest income in Other income and deductions on its Statement of Income.

PECO accounts for uncertain income tax positions in accordance with FERC's guidance on Accounting and Financial Reporting for Uncertainty in Income Taxes, issued in Docket No. AI07-2-000 for FERC reporting purposes. The guidance requires, among other things, that entities should continue to recognize deferred income taxes for FERC accounting and reporting purposes based on the difference between positions taken in tax returns filed or expected to be filed and amounts reported in financial statements.

Pursuant to the Internal Revenue Code and relevant state taxing authorities, Exelon and its subsidiaries, including PECO, file consolidated or combined income tax returns for Federal and certain state jurisdictions where allowed or required. See Note 9—Income Taxes for additional information.

PECO is a party to an agreement (Tax Sharing Agreement) with Exelon that provides for the allocation of consolidated tax liabilities and benefits. The Tax Sharing Agreement generally provides that each party is allocated an amount of tax similar to that which would be owed had the party been separately subject to tax. Any net benefit attributable to the parent is reallocated to other members. That allocation is treated as a contribution to the capital of the party receiving the benefit.

**Taxes Directly Imposed on Revenue-Producing Transactions**

PECO collects certain taxes from customers such as sales and gross receipts taxes, along with other taxes, surcharges, and fees that are levied by state or local governments on the sale or distribution of gas and electricity. Some of these taxes are imposed on the customer, but paid by PECO, while others are imposed on PECO. Where these taxes are imposed on the customer, such as sales taxes, they are reported on a net basis with no impact to the Statement of Income. However, where these taxes are imposed on PECO, such as gross receipts taxes or other surcharges or fees, they are reported on a gross basis. Accordingly, revenues are recognized for the taxes collected from customers along with an offsetting expense. See Note 15—Supplemental Financial Information for PECO's utility taxes that are presented on a gross basis.

**Cash and Cash Equivalents**

PECO considers investments purchased with an original maturity of three months or less to be cash equivalents.

**Restricted Cash and Investments**

Restricted cash and investments recorded in Account 134 represent restricted funds to satisfy designated current liabilities. As of December 31, 2017 and 2016, PECO's restricted cash primarily represented funds from the sales of assets that were subject to PECO's mortgage indenture. PECO's restricted cash is not available for general operations until released from the mortgaged indenture.

Restricted cash and cash equivalents not available to satisfy current liabilities are classified as noncurrent assets.

**Allowance for Uncollectible Accounts**

The allowance for uncollectible accounts reflects PECO's best estimates of losses on the customers' accounts receivable balances. PECO estimates the allowance for uncollectible accounts on customer receivables by applying loss rates developed specifically for PECO to the outstanding receivable balance by customer risk segment. Risk segments represent a group of customers with similar credit quality indicators that are computed based on various attributes, including delinquency of their balances and payment history. Loss rates applied to the accounts receivable balances are based on a historical average of charge-offs as a percentage of accounts receivable in each risk segment. Customers' accounts are generally considered delinquent if the amount billed is not received by the time the next bill is issued, which normally occurs on a monthly basis. Customer accounts are written off consistent with approved regulatory requirements. PECO's provisions for uncollectible accounts will continue to be affected by changes in volume, prices and economic conditions as well as changes in PAPUC regulations.

**Variable Interest Entities**

PECO accounts for its investments in and arrangements with VIEs based on the authoritative guidance which includes the following specific requirements:

- requires an entity to qualitatively assess whether it should consolidate a VIE based on whether the entity has a controlling financial interest, meaning (1) has the power to direct the activities that most significantly impact the VIE's economic performance, and (2) has the obligation to absorb losses or the right to receive benefits of the VIE that could potentially be significant to the VIE,
- requires an ongoing reconsideration of this assessment instead of only upon certain triggering events, and
- requires the entity that consolidates a VIE (the primary beneficiary) to disclose (1) the assets of the consolidated VIE, if they can be used to only settle specific obligations of the consolidated VIE, and (2) the liabilities of a consolidated VIE for which creditors do not have recourse to the general credit of the primary beneficiary.

PECO does not have any significant VIEs.

**Inventories**

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Inventory is recorded at the lower of weighted average cost or net realizable value. Provisions are recorded for excess and obsolete inventory.

***Gas.*** Gas inventory includes the weighted average costs of stored natural gas and propane. The costs of natural gas and propane are generally included in inventory when purchased and charged to purchased power and fuel expense at weighted average cost when used or sold. PECO has several long-term storage contracts for natural gas as well as a liquefied natural gas storage facility.

***Materials and Supplies.*** Materials and supplies inventory generally includes transmission, distribution and generating plant materials. Materials are generally charged to inventory when purchased and expensed or capitalized to property, plant and equipment, as appropriate, at weighted average when installed or used.

**Marketable Securities**

All marketable securities are reported at fair value. Unrealized gains and losses, net of tax, for PECO's available-for-sale securities are reported in Other comprehensive income (OCI). Beginning January 1, 2018, the authoritative guidance eliminates the available-for-sale classification for equity securities and requires that all equity investments (other than those accounted for using the equity method of accounting) be measured and recorded at fair value with any changes in fair value recorded through earnings. The new authoritative guidance does not impact the classification or measurement of investments in debt securities.

**Property, Plant and Equipment**

Property, plant and equipment is recorded at original cost. Original cost includes construction-related direct labor and materials, and when appropriate allowance for funds used during construction (AFUDC) for regulated property at ComEd. The cost of repairs and maintenance, including planned major maintenance activities and minor replacements of property, is charged to Operating and maintenance expense as incurred. ComEd also capitalizes indirect construction costs including labor and related costs of departments associated with supporting construction activities.

Third parties reimburse PECO for all or a portion of expenditures for certain capital projects. Such contributions in aid of construction costs (CIAC) are recorded as a reduction to Property, Plant and Equipment. The U.S. Department of Energy (DOE) smart grid investment grant (SGIG) and other funds reimbursed to PECO by the DOE are accounted for as CIAC.

Upon retirement, the cost of property, net of salvage, is charged to accumulated depreciation consistent with the composite and group methods of depreciation. Removal costs are capitalized to accumulated depreciation when incurred and recorded to depreciation expense over the life of the new asset constructed consistent with PECO's regulatory recovery method.

See Note 4—Property, Plant and Equipment for additional information regarding property, plant and equipment.

**Capitalized Software Costs**

Costs incurred during the application development stage of software projects that are internally developed or purchased for operational use are capitalized within Property, plant, and equipment. Such capitalized amounts are

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amortized ratably over the expected lives of the projects when they become operational, generally not to exceed five years. Certain other capitalized software costs are being amortized over longer lives based on the expected life or pursuant to prescribed regulatory requirements. At December 31, 2017 and 2016, PECO's net unamortized capitalized software costs were $111 million and $91 million, respectively. During the years ended 2017 and 2016, PECO's amortization of capitalized software costs were $39 million and $33 million, respectively.

**Depreciation and Amortization**

Depreciation is generally recorded over the estimated service lives of property, plant and equipment on a straight-line basis using the group, composite or unitary methods of depreciation. The group approach is typically for groups of similar assets that have approximately the same useful lives and the composite approach is used for dissimilar assets that have different lives. Under both methods, a reporting entity depreciates the assets over the average life of the assets in the group. PECO's depreciation expense includes the estimated cost of dismantling and removing plant from service upon retirement, which is consistent with each utility's regulatory recovery method. The estimated service lives for PECO is primarily based on its most recent depreciation studies of historical asset retirement and removal cost experience. See Note 4 — Property, Plant and Equipment for further information regarding depreciation.

Amortization of regulatory assets and liabilities are recorded over the recovery or refund period specified in the related legislation or regulatory order or agreement. When the recovery or refund period is less than one year, amortization is recorded to the line item in which the deferred cost or income would have originally been recorded in PECO's Statement of Income. Amortization of PECO's transmission formula rate regulatory assets are recorded to Operating revenues. With the exception of income tax-related regulatory assets, when the recovery period is more than one year, the amortization is recorded to Depreciation and amortization (Account 403) in PECO's Statement of Income. For income tax related regulatory assets, amortization is generally recorded to Income tax expense (Account 409.1) in PECO's Statement of Income. See Note 2—Regulatory Matters for additional information regarding PECO's regulatory assets.

**Asset Retirement Obligations**

The authoritative guidance for accounting for AROs requires the recognition of a liability for a legal obligation to perform an asset retirement activity even though the timing and/or method of settlement may be conditional on a future event. The liabilities associated with PECO's AROs are adjusted on an ongoing rotational basis, at least once every five years unless circumstances warrant more frequent updates. Changes to the recorded value of an ARO result from the passage of new laws and regulations, revisions to either the timing or amount of estimates of undiscounted cash flows, and estimates of cost escalation factors. AROs are accreted throughout each year to reflect the time value of money for these present value obligations through a charge to operating and maintenance expense in the Statement of Income or, in the case of the majority of PECO's accretion, through an increase to regulatory assets. See Note 10—Asset Retirement Obligations for additional information.

**AFUDC**

PECO applies the authoritative guidance for accounting for certain types of regulation to calculate AFUDC, which is the cost, during the period of construction, of debt and equity funds used to finance construction projects for regulated operations. AFUDC is recorded to construction work in progress and as a non-cash credit to AFUDC that is included in Account 432, Allowance for borrowed funds used during construction - credit, for debt-related funds and Account 419.1, Allowance for other funds used during construction, for equity-related funds. The rates used for capitalizing AFUDC are computed under a method prescribed by regulatory authorities. During 2017 and 2016, credits to AFUDC debt and equity

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were $12 million and $11 million, respectively.

**Guarantees**

PECO recognizes, at the inception of a guarantee, a liability for the fair market value of the obligations it has undertaken by issuing the guarantee, including the ongoing obligation to perform over the term of the guarantee in the event that the specified triggering events or conditions occur.

The liability that is initially recognized at the inception of the guarantee is reduced as PECO is released from risk under the guarantee. Depending on the nature of the guarantee, PECO's release from risk may be recognized only upon the expiration or settlement of the guarantee or by a systematic and rational amortization method over the term of the guarantee.

**Asset Impairments**

PECO evaluates the carrying value of its long-lived assets or asset groups when circumstances indicate the carrying value of those assets may not be recoverable. Indicators of impairment may include a deteriorating business climate, including, but not limited to, declines in energy prices, condition of the asset, specific regulatory disallowance, or plans to dispose of a long-lived asset significantly before the end of its useful life. PECO determines if long-lived assets and asset groups are impaired by comparing the undiscounted expected future cash flows to the carrying value. When the undiscounted cash flow analysis indicates a long-lived asset or asset group is not recoverable, the amount of the impairment loss is determined by measuring the excess of the carrying amount of the long-lived asset or asset group over its fair value.

**Derivative Financial Instruments**

PECO has entered into derivative natural gas contracts to hedge its long-term price risk in the natural gas market. PECO has entered into derivative contracts to procure electric supply through a competitive RFP process as outlined in its PAPUC-approved Default Service Provider Program (DSP Program). PECO does not enter into derivatives for proprietary trading purposes. PECO's derivative activities are in accordance with Exelon's Risk Management Policy.

All derivatives are recognized on the balance sheet at their fair value unless they qualify for certain exceptions, including the normal purchases and normal sales scope exception. Additionally, derivatives that qualify and are designated for hedge accounting are classified as either hedges of the fair value of a recognized asset or liability or of an unrecognized firm commitment (fair value hedge) or hedges of a forecasted transaction or the variability of cash flows to be received or paid related to a recognized asset or liability (cash flow hedge). Cash inflows and outflows related to derivative instruments are included as a component of operating, investing or financing cash flows in the Statement of Cash Flows, depending on the underlying nature of the PECO's hedged items.

Revenues and expenses on derivative contracts that qualify, and are designated, as normal purchases and normal sales are recognized when the underlying physical transaction is completed. While these contracts are considered derivative financial instruments, they are not required to be recorded at fair value, but rather are recorded on an accrual basis of accounting. Normal purchases and normal sales are contracts where physical delivery is probable, quantities are expected to be used or sold in the normal course of business over a reasonable period of time and will not be financially

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settled. If it were determined that a transaction designated as a normal purchase or a normal sale no longer met the exceptions, the fair value of the related contract would be recorded on the balance sheet and offset by a regulatory asset or liability. See Note 8-Derivative Financial Instruments for additional information.

**Retirement Benefits**

PECO participates in Exelon's defined benefit pension plans and other postretirement plans. The measurement of the plan obligations and costs of providing benefits under these plans involve various factors, including numerous assumptions and inputs and accounting elections. The assumptions are reviewed annually and at any interim remeasurement of the plan obligations. The impact of assumption changes or experience different from that assumed on pension and other postretirement benefit obligations is recognized over time rather than immediately recognized in the Statement of Income. Gains or losses in excess of the greater of ten percent of the projected benefit obligation or the market related value (MRV) of plan assets are amortized over the expected average remaining service period of plan participants. See Note 11—Retirement Benefits for additional discussion of PECO's accounting for retirement benefits.

**New Accounting Pronouncements**

***New Accounting Standards Issued and Adopted as of January 1, 2018:*** The following new authoritative accounting guidance issued by the FASB has been adopted as of January 1, 2018 and will be reflected by PECO in the consolidated financial statements beginning in the first quarter of 2018. Unless otherwise indicated, adoption of the new guidance in each instance will have no or insignificant impacts on PECO's Statements of Income, Statements of Cash Flows, Balance Sheets and disclosures.

*Revenue from Contracts with Customers (Issued May 2014 and subsequently amended to address implementation questions; Adopted January 1, 2018):* Changes the criteria for recognizing revenue from a contract with a customer. The new revenue recognition guidance, including subsequent amendments, is effective for annual reporting periods beginning on or after December 15, 2017, with the option to early adopt the standard for annual periods beginning on or after December 15, 2016. PECO did not early adopt this standard.

The new standard replaces existing guidance on revenue recognition, including most industry specific guidance, with a five-step model for recognizing and measuring revenue from contracts with customers. The objective of the new standard is to provide a single, comprehensive revenue recognition model for all contracts with customers to improve comparability within industries, across industries, and across capital markets. The underlying principle is that an entity will recognize revenue to depict the transfer of goods or services to customers at an amount that the entity expects to be entitled to in exchange for those goods or services. The guidance also requires a number of disclosures regarding the nature, amount, timing, and uncertainty of revenue and the related cash flows. The guidance can be applied retrospectively to each prior reporting period presented (full retrospective method) or retrospectively with a cumulative effect adjustment to retained earnings for initial application of the guidance at the date of initial adoption (modified retrospective method). PECO will apply the new guidance using the full retrospective method, which will not have a material impact on previously issued financial statements.

In coordination with the AICPA Power and Utilities Industry Task Force, PECO reached conclusions on the following key accounting issues:

- PECO's tariff sale contracts, including those with lower credit quality customers, are generally deemed to be probable of collection under the guidance and, thus, the timing of revenue recognition will continue to be concurrent with the delivery of electricity or natural gas, consistent with current practice;

- Consistent with current industry practice, revenues recognized from sales of bundled energy commodities (i.e., contracts involving the delivery of multiple energy commodities such as electricity, capacity, ancillary services, etc.) are generally expected to be recognized upon delivery to the customer in an amount based on the invoice price given that it corresponds directly with the value of the commodities transferred to the customer; and

- Contributions in aid of construction are outside of the scope of the standard and, therefore, will continue to be accounted for as a reduction to Property, Plant, and Equipment.

In assessing the impacts of the new revenue guidance, PECO identified the following items that will be accounted for differently:

- Costs to acquire certain contracts (e.g., sales commissions associated with retail power contracts) will be deferred and amortized ratably over the term of the contract rather than being expensed as incurred; and

- Variable consideration within certain contracts (e.g., performance bonuses) will be estimated and recognized as revenue over the term of the contract rather than being recognized when realized.

Based on an assessment of existing contracts and revenue streams, the new guidance, including the identified changes above, will not have a material impact on the amount and timing of PECO's revenue recognition.

One of the new disclosure requirements is to present disaggregated revenue into categories that show how economic factors affect the nature, amount, timing, and uncertainty of revenue and cash flows. In order to comply with this new disclosure requirement, PECO will disclose disaggregated revenue by major customer class (i.e., residential and commercial and industrial) separately for electric and gas in the Notes to Financial Statements. In addition, pursuant to the requirements of the new standard, Exelon and the Utility Registrants will present alternative revenue program revenue separately from revenue from contracts with customers on the face of their Statements of Income.

*Recognition and Measurement of Financial Assets and Financial Liabilities (Issued January 2016; Adopted January 1, 2018):* Eliminates the available-for-sale and cost method classification for equity securities and requires that all equity investments (other than those accounted for using the equity method of accounting) be measured and recorded at fair value with any changes in fair value recorded through earnings and, for equity investments without a readily determinable fair value, provides a measurement alternative of cost less impairment plus or minus adjustments for observable price changes in identical or similar assets. In addition, equity investments without readily determinable fair values must be qualitatively assessed for impairment each reporting period and fair value determined if any significant impairment indicators exist. If fair value is less than carrying value, the impairment is recorded through net income immediately in the period in which it is identified. The guidance does not impact the classification or measurement of investments in debt securities. The guidance also amends several disclosure requirements, including requiring i) financial assets and financial liabilities to be presented separately in the balance sheet or note, grouped by measurement category and form, ii) disclosure of the methods and significant assumptions used to estimate fair value or a description of the changes in the methods and assumptions used to estimate fair value, and iii) for financial assets and liabilities measured at amortized cost, disclosure of the fair value of the amount that would be received to sell the asset or paid to transfer the liability. The guidance is effective January 1, 2018 and must be applied using a modified retrospective transition approach with a cumulative effect adjustment to retained earnings for initial application of the guidance at the date of adoption. PECO

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recorded an insignificant adjustment to opening retained earnings as of January 1, 2018 related to unrealized gains/losses on available for sale equity securities.

*Statement of Cash Flows: Classification of Certain Cash Receipts and Cash Payments (Issued August 2016; Adopted January 1, 2018) and Restricted Cash (Issued November 2016; Adopted January 1, 2018):* In 2016, the FASB issued two standards impacting the Statement of Cash Flows. The first adds or clarifies guidance on the classification of certain cash receipts and payments on the statement of cash flows as follows: debt prepayment or extinguishment costs, settlement of zero-coupon bonds, contingent consideration payments made after a business combination, proceeds from the settlement of insurance claims, proceeds from the settlement of corporate-owned life insurance policies and bank-owned life insurance policies, distributions received from equity method investees, beneficial interest in securitization transactions, and the application of the predominance principle to separately identifiable cash flows. The second states that amounts generally described as restricted cash and restricted cash equivalents should be included with cash and cash equivalents when reconciling the beginning-of-period and end-of-period total amounts shown on the statement of cash flows (instead of being presented as cash flow activities). The new standards are effective on January 1, 2018 and must be applied on a full retrospective basis. Adoption of the second standard will result in a change in presentation of restricted cash on the face of the Statement of Cash Flows; otherwise this guidance will not have a significant impact on the PECO's Consolidated Statements of Cash Flows and disclosures.

*Intra-Entity Transfers of Assets Other Than Inventory (Issued October 2016; Adopted January 1, 2018):* Requires entities to recognize the income tax consequences of an intra-entity transfer of an asset other than inventory when the transfer occurs (current GAAP prohibits the recognition of current and deferred income taxes for an intra-entity asset transfer until the asset has been sold to an outside party). The standard is effective January 1, 2018 with early adoption permitted. The guidance requires a modified retrospective transition approach through a cumulative-effect adjustment to retained earnings as of the beginning of the period of adoption.

*Clarifying the Definition of a Business (Issued January 2017; Adopted January 1, 2018):* Clarifies the definition of a business with the objective of addressing whether acquisitions (or dispositions) should be accounted for as acquisitions/dispositions of assets or as acquisitions/dispositions of businesses. If substantially all the fair value of the assets acquired/disposed of is concentrated in a single identifiable asset or a group of similar identifiable assets, the set of transferred assets and activities is not a business. If the fair value of the assets acquired/disposed of is not concentrated in a single identifiable asset or a group of similar identifiable assets, then an entity must evaluate whether an input and a substantive process exist, which together significantly contribute to the ability to produce outputs. The standard also revises the definition of outputs to focus on goods and services to customers. The standard will likely result in more acquisitions being accounted for as asset acquisitions. The standard is effective January 1, 2018, with early adoption permitted, and must be applied on a prospective basis. PECO did not early adopt the guidance.

*Improving the Presentation of Net Periodic Pension Cost and Net Periodic Postretirement Benefit Cost (Issued March 2017; Adopted January 1, 2018):* Changes the accounting and presentation of pension and OPEB costs at the plan sponsor (i.e., Exelon) level. The guidance requires plan sponsors to report the service cost and other non-service cost components of net periodic pension cost and net periodic OPEB cost (together, net benefit cost) separately. Under the new guidance, service cost is presented as part of income from operations and the other non-service cost components are classified outside of income from operations on the Consolidated Statements of Operations and Comprehensive Income. Additionally, service cost is the only component eligible for capitalization. Under prior GAAP, the total amount of net benefit cost was recorded as part of income from operations and all components were eligible for capitalization.

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PECO participates in Exelon's single employer pension and OPEB plans and apply multi-employer accounting. Multi-employer accounting is not impacted by this standard; therefore, Exelon's subsidiary financial statements will not change upon its adoption. On Exelon's consolidated financial statements, non-service cost components of pension and OPEB cost capitalizable under a regulatory framework are prospectively reported as regulatory assets (currently, they are capitalizable under pension and OPEB accounting guidance and reported as PP&E). These regulatory assets are amortized outside of operating income.

The presentation of the service cost component and the other non-service cost components of net benefit cost will be applied retrospectively in the Exelon consolidated financial statements beginning in the first quarter of 2018. On Exelon's consolidated financial statements, service cost will continue to be reported in Operating and maintenance and Non-service cost will be reported outside of operating income. The prospective change in the capitalization eligibility is not expected to have a significant impact on Exelon's consolidated net income.

***New Accounting Standards Issued and Not Yet Adopted as of December 31, 2017:*** The following new authoritative accounting guidance issued by the FASB has not yet been adopted and reflected by PECO in the consolidated financial statements as of December 31, 2017. Unless otherwise indicated, the PECO is currently assessing the impacts such guidance may have (which could be material) on the Balance Sheets, Statements of Income, Statements of Cash Flows and disclosures, as well as the potential to early adopt where applicable. PECO has assessed other FASB issuances of new standards which are not listed below given the current expectation such standards will not significantly impact the PECO's financial reporting.

*Leases (Issued February 2016):* Increases transparency and comparability among organizations by recognizing lease assets and lease liabilities on the balance sheet and disclosing key information about leasing arrangements. The standard is effective January 1, 2019. Early adoption is permitted, however PECO will not early adopt the standard. The issued guidance required a modified retrospective transition approach, which requires lessees and lessors to recognize and measure leases at the beginning of the earliest period presented (January 1, 2017). In January 2018, the FASB proposed amending the standard to give entities another option for transition. The proposed transition method would allow entities to initially apply the requirements of the standard in the period of adoption (January 1, 2019). PECO will assess this transition option when the FASB issues the standard.

The new guidance requires lessees to recognize both the right-of-use assets and lease liabilities in the balance sheet for most leases, whereas today only finance lease liabilities (referred to as capital leases) are recognized in the balance sheet. In addition, the definition of a lease has been revised when an arrangement conveys the right to control the use of the identified asset which may change the classification of an arrangement as a lease. Quantitative and qualitative disclosures related to the amount, timing and judgments of an entity's accounting for leases and the related cash flows are also expanded. Disclosure requirements apply to both lessees and lessors, whereas current disclosures relate only to lessees. Significant changes to lease systems, processes and procedures are required to implement the requirements of the new standard. The recognition, measurement, and presentation of expenses and cash flows arising from a lease by a lessee have not significantly changed from current GAAP. Lessor accounting is also largely unchanged.

The standard provides a number of transition practical expedients that entities may elect. These include a "package of three" expedients that must be taken together and allow entities to (1) not reassess whether existing contracts contain leases, (2) carryforward the existing lease classification, and (3) not reassess initial direct costs associated with existing leases. In January 2018, the FASB issued additional guidance which provides another optional transition practical expedient. This practical expedient allows entities to not evaluate land easements under the new guidance at adoption if they were not previously accounted for as leases.

PECO has assessed the lease standard and are executing a detailed implementation plan in preparation for adoption on January 1, 2019. Key activities in the implementation plan include:

- Developing a complete lease inventory and abstracting the required data attributes into a lease accounting system that supports PECO's lease portfolios and integrates with existing systems.
- Evaluating the transition practical expedients available under the guidance.
- Identifying, assessing and documenting technical accounting issues, policy considerations and financial reporting implications. Includes completing a detailed contract assessment for a sample of transactions to determine whether they are leases under the new guidance.
- Identifying and implementing changes to processes and controls to ensure all impacts of the new guidance are effectively addressed.

Accounting and implementation issues continue to be identified and evaluated by the implementation team.

*Impairment of Financial Instruments (Issued June 2016):* Provides for a new Current Expected Credit Loss (CECL) impairment model for specified financial instruments including loans, trade receivables, debt securities classified as held-to-maturity investments and net investments in leases recognized by a lessor. Under the new guidance, on initial recognition and at each reporting period, an entity is required to recognize an allowance that reflects the entity's current estimate of credit losses expected to be incurred over the life of the financial instrument. The standard does not make changes to the existing impairment models for non-financial assets such as fixed assets, intangibles and goodwill. The standard will be effective January 1, 2020 (with early adoption as of January 1, 2019 permitted) and, for most debt instruments, requires a modified retrospective transition approach through a cumulative-effect adjustment to retained earnings as of the beginning of the period of adoption.

*Goodwill Impairment (Issued January 2017):* Simplifies the accounting for goodwill impairment by removing Step 2 of the current test, which requires calculation of a hypothetical purchase price allocation. Under the revised guidance, goodwill impairment will be measured as the amount by which a reporting unit's carrying value exceeds its fair value, not to exceed the carrying amount of goodwill (currently Step 1 of the two-step impairment test). Entities will continue to have the option to perform a qualitative assessment to determine if a quantitative impairment test is necessary. This updated guidance is not currently expected to impact PECO's financial reporting. The standard is effective January 1, 2020, with early adoption permitted, and must be applied on a prospective basis.

*Derivatives and Hedging (Issued September 2017):* Allows more financial and nonfinancial hedging strategies to be eligible for hedge accounting. The amendments are intended to more closely align hedge accounting with companies' risk management strategies, simplify the application of hedge accounting, and increase transparency as to the scope and results of hedging programs. There are also amendments related to effectiveness testing and disclosure requirements. The guidance is effective January 1, 2019 and early adoption is permitted with a modified retrospective transition approach. PECO is currently assessing this standard but does not currently expect a significant impact given the limited activity for which PECO elects hedge accounting and because PECO does not anticipate increasing its use of hedge accounting as a result of this standard.

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**1. Significant Accounting Policies**

**Description of Business**

Incorporated in Pennsylvania in 1929, PECO Energy Company (PECO) is engaged principally in the purchase and regulated retail sale of electricity and the provision of transmission and distribution services to residential, commercial and industrial customers in southeastern Pennsylvania, including the City of Philadelphia, as well as the purchase and regulated retail sale of natural gas and the provision of distribution services to residential, commercial and industrial customers in the Pennsylvania counties surrounding the City of Philadelphia. PECO is subject to extensive regulation by the Pennsylvania Public Utility Commission (PAPUC) as to electric and gas distribution rates and service, the issuances of certain securities and certain other aspects of PECO's operations. PECO is a public utility under the Federal Power Act subject to regulation by the Federal Energy Regulatory Commission (FERC) as to transmission rates and certain other aspects of PECO's business and by the U.S. Department of Transportation as to pipeline safety and other aspects of gas operations. Additionally, PECO is also subject to the North American Electric Reliability Corporation (NERC) mandatory reliability standards. Pursuant to the Pennsylvania Electricity Generation Customer Choice and Competition Act of 1996 (Competition Act), the Commonwealth of Pennsylvania required the unbundling of retail electric services in Pennsylvania into separate energy transmission and distribution services with open retail competition for generation services. PECO serves as the local distribution company providing electric distribution services in its franchised service territory in southeastern Pennsylvania and energy service to customers who do not choose a competitive electric generation supplier or who choose to return to the utility after taking service from a competitive electric generation supplier.

**Basis of Presentation**

PECO is a principal indirect subsidiary of Exelon Corporation (Exelon), which indirectly owns 100% of PECO's common stock. At December 31, 2018 and 2017, PECO's common stock without par value consisted of 500,000,000 shares authorized and 170,478,507 shares outstanding.

Accounting policies for regulated operations are in accordance with those prescribed by the regulatory authorities having jurisdiction, principally the PAPUC and FERC. The accompanying financial statements have been prepared in accordance with the accounting requirements of FERC as set forth in the Uniform System of Accounts (USOA) and accounting releases, which differ from accounting principles generally accepted in the United States of America (GAAP). The principal differences from GAAP include the exclusions of current maturities of long-term debt from current liabilities, the exclusion of debt issuance costs from long-term debt, the requirement to report deferred tax assets and liabilities separately rather than as a single amount, the classification of accrued taxes as assets and liabilities rather than a net amount, the exclusion of FIN 48 liabilities related to temporary income tax differences, and the classification of certain other assets and liabilities as current instead of noncurrent.

PECO consolidates the accounts of entities in which PECO has a controlling financial interest, after the elimination of intercompany transactions. Where PECO does not have a controlling financial interest in an entity, proportionate consolidation, equity method accounting or accounting for investments in equity securities without readily determinable fair value is applied. PECO applies proportionate consolidation when they have an undivided interest in an asset and are proportionately liable for their share of each liability associated with the asset. PECO proportionately consolidates their undivided ownership interests in jointly owned electric plants and transmission facilities. Under proportionate consolidation, PECO separately records their proportionate share of the assets, liabilities, revenues and expenses related to the undivided interest in the asset. PECO applies equity method accounting when they have significant influence over an investee through an ownership in common stock, which generally approximates a 20% to 50% voting interest. PECO applies equity method accounting to certain investments and joint ventures, including certain financing trusts. Under equity method accounting, PECO reports their interest in the entity as an investment and PECO's percentage share of the earnings from the entity as single line items in their financial statements. PECO uses accounting for investments in equity securities without readily determinable fair values if they lack significant influence, which generally results when they hold less than 20% of the common stock of an entity. Under accounting for investments in equity securities without readily determinable fair values, PECO reports their investments at cost adjusted for changes from observable transactions for identical or similar investments of the same issuer, less impairment. Changes in measurement are reported in earnings.

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PECO's investments in its subsidiaries, ExTel Corporation, LLC, PECO Wireless, LLC, PECO Energy Capital Trust IV (PECO Trust IV) and PECO Energy Capital Corporation (PECC) are accounted for under the equity method of accounting in accordance with the USOA. PECO Wireless, LLC is the parent company of ATNP Finance Company and sole member of PEC Financial Services, LLC. PECC is the general partner of PECO Energy Capital, L.P., which is the grantor of PECO Energy Capital Trust III (PECO Trust III). ExTel Corporation, LLC and PECO Wireless, LLC are consolidated in PECO's GAAP Financial Statements.

**Use of Estimates**

The preparation of financial statements of PECO in conformity with GAAP requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Areas in which significant estimates have been made include, but are not limited to, the accounting for nuclear decommissioning costs and other AROs, pension and other postretirement benefits, the application of purchase accounting, inventory reserves, allowance for uncollectible accounts, goodwill and asset impairments, derivative instruments, unamortized energy contracts, fixed asset depreciation, environmental costs and other loss contingencies, taxes and unbilled energy revenues. Actual results could differ from those estimates.

**Accounting for the Effects of Regulation**

For their regulated electric and gas operations, PECO reflects the effects of cost-based rate regulation in their financial statements, which is required for entities with regulated operations that meet the following criteria: 1) rates are established or approved by a third-party regulator; (2) rates are designed to recover the entities' cost of providing services or products; and (3) there is a reasonable expectation that rates designed to recover costs can be charged to and collected from customers. Regulatory assets and liabilities are amortized and the related expense or revenue is recognized in the Statement of Income consistent with the recovery or refund included in customer rates. PECO's regulatory assets and liabilities as of the balance sheet date are probable of being recovered or settled in future rates. If a separable portion of PECO's business was no longer able to meet the criteria discussed above, the affected entities would be required to eliminate from its financial statements the effects of regulation for that portion, which could have a material impact on their financial statements. See Note 2—Regulatory Matters for additional information.

With the exception of income tax-related regulatory assets and liabilities, PECO classifies regulatory assets and liabilities with a recovery or settlement period greater than one year as both current and non- current in its Balance Sheet, with the current portion representing the amount expected to be recovered from or settled to customers over the next twelve-month period as of the balance sheet date. Income tax-related regulatory assets and liabilities are classified entirely as non-current in PECO's Balance Sheets to align with the classification of the related deferred income tax balances.

PECO treats the impacts of a final rate order received after the balance sheet date but prior to the issuance of the financial statements as a non-recognized subsequent event, as the receipt of a final rate order is a separate and distinct event that has future impacts on the parties affected by the order.

**Revenues**

**Operating Revenues.** PECO's operating revenues generally consist of revenues from contracts with customers involving the sale and delivery of energy commodities and related products and services, utility revenues from alternative revenue programs (ARP), and realized and unrealized revenues recognized under mark-to-market energy commodity derivative contracts. PECO recognizes revenue from contracts with customers to depict the transfer of goods or services to customers in an amount that the entities expect to be entitled to in exchange for those goods or services. PECO's primary sources of revenue include regulated electric and natural gas tariff sales, distribution and transmission services. At the end of each month, PECO accrues an estimate for the unbilled amount of energy delivered or services provided to customers.

PECO records ARP revenue for its best estimate of the transmission revenue impacts resulting from future changes in rates that they believe are probable of approval by FERC in accordance with their formula rate mechanisms. See Note 2—Regulatory Matters and

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Note 14—Supplemental Financial Information for additional information.

**Option Contracts, Swaps and Commodity Derivatives**. Certain option contracts and swap arrangements that meet the definition of derivative instruments are recorded at fair value with subsequent changes in fair value recognized as revenue or expense. The classification of revenue or expense is based on the intent of the transaction. To the extent PECO receives full cost recovery for energy procurement and related costs from retail customers, it records the fair value of its energy swap contracts with unaffiliated suppliers as well as an offsetting regulatory asset or liability in its Balance Sheets. See Note 2—Regulatory Matters and Note 6—Derivative Financial Instruments for additional information.

**Taxes Directly Imposed on Revenue-Producing Transactions**. PECO collects certain taxes from customers such as sales and gross receipts taxes, along with other taxes, surcharges and fees, that are levied by state or local governments on the sale or distribution of gas and electricity. Some of these taxes are imposed on the customer, but paid by PECO, while others are imposed on the Registrants. Where these taxes are imposed on the customer, such as sales taxes, they are reported on a net basis with no impact to the Statements of Income. However, where these taxes are imposed on PECO, such as gross receipts taxes or other surcharges or fees, they are reported on a gross basis. Accordingly, revenues are recognized for the taxes collected from customers along with an offsetting expense. See Note 14 — Supplemental Financial Information for PECO's utility taxes that are presented on a gross basis.

**Income Taxes**

Deferred Federal and state income taxes are recorded on significant temporary differences between the book and tax basis of assets and liabilities and for tax benefits carried forward. Investment tax credits have been deferred in PECO's Balance Sheets and are recognized in book income over the life of the related property. PECO accounts for uncertain income tax positions using a benefit recognition model with a two-step approach; a more-likely-than-not recognition criterion; and a measurement approach that measures the position as the largest amount of tax benefit that is greater than 50% likely of being realized upon ultimate settlement. If it is not more-likely-than-not that the benefit of the tax position will be sustained on its technical merits, no benefit is recorded. Uncertain tax positions that relate only to timing of when an item is included on a tax return are considered to have met the recognition threshold. PECO recognizes accrued interest related to unrecognized tax benefits in Interest expense or Other income and deductions (interest income) and recognize penalties related to unrecognized tax benefits in Other, net in their Statements of Income.

Pursuant to the IRC and relevant state taxing authorities, PECO and its subsidiaries file or combined income tax returns for Federal and certain state jurisdictions where allowed or required. See Note 8 - Income Taxes for additional information.

**Cash and Cash Equivalents**

PECO considers investments purchased with an original maturity of three months or less to be cash equivalents.

**Restricted Cash and Investments**

Restricted cash and investments recorded in Account 134 represent restricted funds to satisfy designated current liabilities. As of December 31, 2018 and 2017, PECO's restricted cash primarily represented funds from the sales of assets that were subject to PECO's mortgage indenture.

**Allowance for Uncollectible Accounts**

The allowance for uncollectible accounts reflects PECO's best estimates of losses on the customers' accounts receivable balances. PECO estimates the allowance by applying loss rates developed specifically for each company to the outstanding receivable balance by customer risk segment. PECO's customer accounts are written off consistent with approved regulatory requirements.

**Variable Interest Entities**

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PECO accounts for its investments in and arrangements with VIEs based on the following specific requirements:

- requires an entity to qualitatively assess whether it should consolidate a VIE based on whether the entity has a controlling financial interest,
- requires an ongoing reconsideration of this assessment instead of only upon certain triggering events, and
- requires the entity that consolidates a VIE (the primary beneficiary) to disclose (1) the assets of the VIE, if they can be used to only settle specific obligations of the VIE, and (2) the liabilities of a VIE for which creditors do not have recourse to the general credit of the primary beneficiary.

PECO does not have any significant VIEs.

**Inventories**

Inventory is recorded at the lower of weighted average cost or net realizable value. Provisions are recorded for excess and obsolete inventory. Fossil fuel, materials and supplies, and emissions allowances are generally included in inventory when purchased. Fossil fuel and emissions allowances are expensed to purchased power and fuel expense when used or sold. Materials and supplies generally includes transmission, distribution and generating plant materials and are expensed to operating and maintenance or capitalized to property, plant and equipment, as appropriate, when installed or used.

**Debt and Equity Security Investments**

***Equity Security Investments with Readily Determinable Fair Values.*** Equity securities held in the NDT funds are classified as equity securities with readily determinable fair values. Realized and unrealized gains and losses, net of tax, on Generation's NDT funds associated with the Regulatory Agreement Units are included in regulatory liabilities at PECO and in Noncurrent payables to affiliates at Generation and in Noncurrent receivables from affiliates at PECO. See Note 2—Regulatory Matters for additional information regarding PECO's regulatory assets and liabilities and Note 5—Fair Value of Financial Assets and Liabilities and Note 9—Asset Retirement Obligations for additional information regarding marketable securities held by NDT funds.

**Property, Plant and Equipment**

Property, plant and equipment is recorded at original cost. Original cost includes construction-related direct labor and material costs. PECO also includes indirect construction costs including labor and related costs of departments associated with supporting construction activities. When appropriate, original cost also includes capitalized interest for Generation, Exelon Corporate and PHI and AFUDC for regulated property at PECO. The cost of repairs and maintenance, including planned major maintenance activities and minor replacements of property, is charged to Operating and maintenance expense as incurred.

Third parties reimburse PECO for all or a portion of expenditures for certain capital projects. Such contributions in aid of construction costs (CIAC) are recorded as a reduction to Property, plant and equipment, net. DOE SGIG and other funds reimbursed to PECO have been accounted for as CIAC.

Upon retirement, the cost of property, net of salvage, is charged to accumulated depreciation consistent with the composite and group methods of depreciation. Removal costs are capitalized to accumulated depreciation when incurred and recorded to depreciation expense over the life of the new asset constructed consistent with PECO's regulatory recovery method.

See Note 3—Property, Plant and Equipment for additional information regarding property, plant and equipment.

**Capitalized Software Costs**

Costs incurred during the application development stage of software projects that are internally developed or purchased for operational use are capitalized within Property, plant, and equipment. Such capitalized amounts are amortized ratably over the expected lives of the projects when they become operational, generally not to exceed five years. Certain other capitalized software costs are being amortized over longer lives based on the expected life or pursuant to prescribed regulatory requirements.

**Depreciation and Amortization**

Depreciation is generally recorded over the estimated service lives of property, plant and equipment on a straight-line basis using the group, composite or unitary methods of depreciation. The group approach is typically for groups of similar assets that have approximately the same useful lives and the composite approach is used for dissimilar assets that have different lives. Under both methods, a reporting entity depreciates the assets over the average life of the assets in the group. PECO's depreciation expense includes the estimated cost of dismantling and removing plant from service upon retirement, which is consistent with each utility's regulatory recovery method. The estimated service lives for PECO is primarily based on its most recent depreciation studies of historical asset retirement and removal cost experience. See Note 3—Property, Plant and Equipment for further information regarding depreciation.

Amortization of regulatory assets and liabilities are recorded over the recovery or refund period specified in the related legislation or regulatory order or agreement. When the recovery or refund period is less than one year, amortization is recorded to the line item in which the deferred cost or income would have originally been recorded in PECO's Statement of Income. Amortization of PECO's transmission formula rate regulatory assets are recorded to Operating revenues. Amortization of income tax related regulatory assets and liabilities is generally recorded to Income tax expense. With the exception of income tax-related regulatory assets, when the recovery period is more than one year, the amortization is recorded to Depreciation and amortization (Account 403) in PECO's Statement of Income. For income tax related regulatory assets, amortization is generally recorded to Income tax expense (Account 409.1) in PECO's Statement of Income. See Note 2—Regulatory Matters for additional information regarding PECO's regulatory assets.

**Asset Retirement Obligations**

AROs are accreted throughout each year to reflect the time value of money for these present value obligations through an increase to regulatory assets. See Note 9—Asset Retirement Obligations for additional information.

**Guarantees**

PECO recognizes, at the inception of a guarantee, a liability for the fair market value of the obligations it has undertaken by issuing the guarantee, including the ongoing obligation to perform over the term of the guarantee in the event that the specified triggering events or conditions occur.

The liability that is initially recognized at the inception of the guarantee is reduced as PECO is released from risk under the guarantee. Depending on the nature of the guarantee, PECO's release from risk may be recognized only upon the expiration or settlement of the guarantee or by a systematic and rational amortization method over the term of the guarantee. See Note 13—Commitments and Contingencies for additional information.

**Asset Impairments**

***Long-Lived Assets.*** PECO evaluates the carrying value of its long-lived assets or asset groups when circumstances indicate the carrying value of those assets may not be recoverable. Indicators of impairment may include a deteriorating business climate, including, but not limited to, declines in energy prices, condition of the asset, specific regulatory disallowance, or plans to dispose of a long-lived asset significantly before the end of its useful life. PECO determines if long-lived assets and asset groups are impaired by comparing the undiscounted expected future cash flows to the carrying value. When the undiscounted cash flow analysis indicates a long-lived asset or asset group is not recoverable, the amount of the impairment loss is determined by measuring the excess of the carrying amount of the long-lived asset or asset group over its fair value. See Note 9—Asset Retirement Obligations for additional information.

**Derivative Financial Instruments**

PECO has entered into derivative natural gas contracts to hedge its long-term price risk in the natural gas market. PECO has entered into derivative contracts to procure electric supply through a competitive RFP process as outlined in its PAPUC-approved Default Service Provider Program (DSP Program). PECO does not enter into derivatives for proprietary trading purposes. PECO's derivative activities are in accordance with Exelon's Risk Management Policy.

All derivatives are recognized on the balance sheet at their fair value unless they qualify for certain exceptions, including the normal purchases and normal sales exception. For derivatives intended to serve as economic hedges, changes in fair value are recognized in earnings each period. Amounts classified in earnings are included in Operating revenue, Purchased power and fuel, Interest expense or Other, net in the Statements of Operations and Comprehensive Income based on the activity the transaction is economically hedging. While the majority of the derivatives serve as economic hedges, there are also derivatives entered into for proprietary trading purposes, subject to Exelon's Risk Management Policy, and changes in the fair value of those derivatives are recorded in revenue in the Statements of Operations and Comprehensive Income. At PECO, changes in fair value may be recorded as a regulatory asset or liability if there is an ability to recover or return the associated costs. Cash inflows and outflows related to derivative instruments are included as a component of operating, investing or financing cash flows in the Statements of Cash Flows, depending on the nature of each transaction. On July 1, 2018, Exelon and Generation de-designated its fair value and cash flow hedges. See Note 2 — Regulatory Matters and Note 6—Derivative Financial Instruments for additional information.

Revenues and expenses on derivative contracts that qualify, and are designated, as normal purchases and normal sales are recognized when the underlying physical transaction is completed. While these contracts are considered derivative financial instruments, they are not required to be recorded at fair value, but rather are recorded on an accrual basis of accounting. See Note 6—Derivative Financial Instruments for additional information.

**Retirement Benefits**

PECO participates in Exelon's defined benefit pension plans and other postretirement plans. The measurement of the plan obligations and costs of providing benefits under these plans involve various factors, including numerous assumptions and inputs and accounting elections. The assumptions are reviewed annually and at any interim remeasurement of the plan obligations. The impact of assumption changes or experience different from that assumed on pension and other postretirement benefit obligations is recognized over time rather than immediately recognized in the Statement of Income. Gains or losses in excess of the greater of ten percent of the projected benefit obligation or the market related value (MRV) of plan assets are amortized over the expected average remaining service period of plan participants. See Note 10—Retirement Benefits for additional discussion of PECO's accounting for retirement benefits.

**New Accounting Standards**

**New Accounting Standards Adopted in 2018:** In 2018, the PECO adopted the following new authoritative accounting guidance issued by the FASB.

*Defined Benefit Plan Disclosures (Issued August 2018).* Eliminates existing disclosure requirements related to amounts in Accumulated other comprehensive income expected to be recognized in Net periodic benefit cost over the next year and the effects of a one-percentage-point change in the assumed health care cost trend rates. In addition, new disclosures were added such as the weighted-average interest crediting rates for cash balance plans and an explanation for the reasons for significant gains and losses related to changes in the benefit obligation. The standard is effective January 1, 2021, with early adoption permitted, and must be applied retrospectively. Exelon early adopted this standard in the fourth quarter of 2018. See Note 10—Retirement Benefits for additional information.

*Fair Value Measurement Disclosures (Issued August 2018).* Updates the disclosure requirements for fair value measurements to improve the usefulness of information for financial statement users. The guidance removes the requirements to disclose (1) the amount of and reasons for transfers between Level 1 and Level 2, (2) the policy for timing of transfers between levels, and (3) the valuation processes for Level 3 fair value measurements and adds a requirement to disclose the range and weighted average of significant unobservable inputs used to develop Level 3 fair value measurements. The standard is effective January 1, 2020, with early adoption permitted. The amendments to remove disclosures must be applied retrospectively and can be early adopted, while the amendments to add disclosures must be applied prospectively and adoption can be delayed until the effective date. PECO early adopted, in the fourth quarter of 2018, the amendments to remove disclosures and will adopt the amendments to add disclosures in the first quarter of 2020. The impact of the new disclosures is not expected to be material to PECO's financial statements. See Note 5—Fair Value of Financial Assets and Liabilities for additional information.

*Improving the Presentation of Net Periodic Pension Cost and Net Periodic Postretirement Benefit Cost (Issued March 2017).* Changes the accounting and presentation of pension and OPEB costs at the plan sponsor (i.e., Exelon) level. The guidance requires plan sponsors to report the service cost and other non-service cost components of net periodic pension cost and net periodic OPEB cost (together, net benefit cost) separately. Under the new guidance, service cost is presented as part of income from operations and the other non-service cost components are classified outside of income from operations in the Statement of Income. Additionally, service cost is the only component eligible for capitalization on a prospective basis beginning on January 1, 2018. Under prior GAAP, the total amount of net benefit cost was recorded as part of income from operations and all components were eligible for capitalization. Exelon applied the presentation of the service component and the other non-service cost components of net benefit costs retrospectively and, accordingly, has recasted those amounts, which were not material, in its Statement of Income in prior periods presented. Exelon elected the practical expedient that permits an employer to use the amounts disclosed in its pension and other postretirement benefit plan note for the comparative periods as the estimation basis for applying the retrospective presentation requirements. In Exelon's consolidated financial statements, non-service cost components of pension and OPEB cost capitalizable under a regulatory framework were prospectively reported as regulatory assets (previously, they were capitalizable under pension and OPEB accounting guidance and reported as PP&E). These regulatory assets are amortized outside of operating income. See Note 10—Retirement Benefits for additional information.

PECO participates in Exelon's single employer pension and OPEB plans and apply multi-employer accounting. Multi-employer accounting was not impacted by this standard; therefore, PECO's financial statements did not change upon its adoption.

*Statement of Cash Flows: Classification of Restricted Cash (Issued November 2016).* The standard states that amounts generally described as restricted cash and restricted cash equivalents should be included with cash and cash equivalents when reconciling the beginning-of-period and end-of-period total amounts shown on the statement of cash flows (instead of being presented as cash flow activities).

*Recognition and Measurement of Financial Assets and Financial Liabilities (Issued January 2016).* Eliminates the available-for-sale and cost method classification for equity securities and requires that all equity investments (other than those accounted for using the equity method of accounting) be measured and recorded at fair value with any changes in fair value recorded through earnings and, for equity investments without a readily determinable fair value, provides a measurement alternative of cost less impairment plus or minus adjustments for observable price changes in identical or similar assets. In addition, equity investments without readily determinable fair values must be qualitatively assessed for impairment each reporting period and fair value determined if any significant impairment indicators exist. If fair value is less than carrying value, the impairment is recorded through net income immediately in the period in which it is identified. The guidance does not impact the classification or measurement of investments in debt securities. The guidance also amends several disclosure requirements, including requiring i) financial assets and financial liabilities to be presented separately in the balance sheet or note, grouped by measurement category and form, ii) disclosure of the methods and significant assumptions used to estimate fair value or a description of the changes in the methods and assumptions used to estimate fair value, and iii) for financial assets and liabilities measured at amortized cost, disclosure of the fair value of the amount that would be received to sell the asset or paid to transfer the liability. The guidance was applied using a modified retrospective transition approach with a cumulative effect adjustment to retained earnings for initial application of the guidance at the date of adoption. PECO recorded an insignificant adjustment to opening retained earnings as of January 1, 2018 related to unrealized gains/losses on available for sale equity securities. See Note 12—Changes in Accumulated Other Comprehensive Income for additional information.

*Revenue from Contracts with Customers (Issued May 2014 and subsequently amended to address implementation questions).* Changes the criteria for recognizing revenue from a contract with a customer. The new standard replaces existing guidance on revenue recognition, including most industry specific guidance, with a five-step model for recognizing and measuring revenue from contracts with customers. The objective of the new standard is to provide a single, comprehensive revenue recognition model for all contracts with customers to improve comparability within industries, across industries, and across capital markets. The underlying principle is that an entity will recognize revenue to depict the transfer of goods or services to customers at an amount that the entity expects to be entitled to in exchange for those goods or services. The guidance also requires a number of disclosures regarding the nature, amount, timing, and uncertainty of revenue and the related cash flows. The guidance can be applied retrospectively to each prior reporting period presented (full retrospective method) or retrospectively with a cumulative effect adjustment to retained earnings for initial application of the guidance at the date of initial adoption (modified retrospective method). The guidance was not adopted for FERC and results in no change to the Statement of Income.

**New Accounting Standards Adopted as of January 1, 2019:** The following new authoritative accounting guidance issued by the FASB was adopted as of January 1, 2019 and will be reflected by PECO in their financial statements beginning in the first quarter of 2019.

*Cloud Computing Arrangements (Issued August 2018).* Aligns the requirements for capitalizing costs incurred to implement a cloud computing arrangement with the internal-use software guidance. As a result, certain implementation costs incurred in a cloud computing arrangement that are currently expensed as incurred will be deferred and amortized over the non-cancellable term of the arrangement plus any reasonably certain renewal periods. The standard is effective January 1, 2020, with early adoption permitted, and can be applied using either a prospective or retrospective transition approach. A retrospective approach requires a cumulative-effect adjustment to retained earnings as of the beginning of the period of adoption. PECO early adopted this standard using a prospective approach as of January 1, 2019. The new guidance is not expected to have a material impact on PECO's financial statements.

*Leases (Issued February 2016).* Increases transparency and comparability among organizations by recognizing lease assets and lease liabilities on the balance sheet and disclosing key information about leasing arrangements. PECO adopted the standard on January 1, 2019.

The new standard requires lessees to recognize both the right-of-use assets and lease liabilities in the balance sheet for most leases, whereas under previous GAAP only finance lease liabilities (referred to as capital leases) were recognized in the balance sheet. In addition, the definition of a lease has been revised which may result in changes to the classification of an arrangement as a lease. Under the new standard, an arrangement that conveys the right to control the use of an identified asset by obtaining substantially all of its economic benefits and directing how it is used is a lease, whereas the previous definition focuses on the ability to control the use of the asset or to obtain its output. Quantitative and qualitative disclosures related to the amount, timing and judgments of an entity's accounting for leases and the related cash flows are expanded. Disclosure requirements apply to both lessees and lessors, whereas previous disclosures related only to lessees. The recognition, measurement, and presentation of expenses and cash flows arising from a lease by a lessee have not significantly changed from previous GAAP. Lessor accounting is also largely unchanged. The guidance was not adopted for FERC reporting purposes and will result in no change to the Balance Sheet in 2019.

**New Accounting Standards Issued and Not Yet Adopted as of December 31, 2018:** The following new authoritative accounting guidance issued by the FASB has not yet been adopted and reflected by PECO in their financial statements as of December 31, 2018. Unless otherwise indicated, the Registrants are currently assessing the impacts such guidance may have (which could be material) in their Balance Sheets, Statements of Income, Statements of Cash Flows and disclosures, as well as the potential to early adopt where applicable. PECO has assessed other FASB issuances of new standards which are not listed below given the

| Name of Respondent | This Report is: | Date of Report (Mo, Da, Yr) | Year/Period of Report |
|---|---|---|---|
| PECO Energy Company | (1) X An Original<br>(2) _ A Resubmission | 03/28/2019 | 2018/Q4 |

NOTES TO FINANCIAL STATEMENTS (Continued)

current expectation that such standards will not significantly impact the Registrants' financial reporting.

*Goodwill Impairment (Issued January 2017).* Simplifies the accounting for goodwill impairment by removing Step 2 of the current test, which requires calculation of a hypothetical purchase price allocation. Under the revised guidance, goodwill impairment will be measured as the amount by which a reporting unit's carrying value exceeds its fair value, not to exceed the carrying amount of goodwill (currently Step 1 of the two-step impairment test). Entities will continue to have the option to perform a qualitative assessment to determine if a quantitative impairment test is necessary. PECO has no goodwill as of December 31, 2018.

*Impairment of Financial Instruments (Issued June 2016).* Provides for a new Current Expected Credit Loss (CECL) impairment model for specified financial instruments including loans, trade receivables, debt securities classified as held-to-maturity investments and net investments in leases recognized by a lessor. Under the new guidance, on initial recognition and at each reporting period, an entity is required to recognize an allowance that reflects the entity's current estimate of credit losses expected to be incurred over the life of the financial instrument. The standard does not make changes to the existing impairment models for non-financial assets such as fixed assets, intangibles and goodwill. The standard will be effective January 1, 2020 (with early adoption as of January 1, 2019 permitted) and requires a modified retrospective transition approach through a cumulative-effect adjustment to retained earnings as of the beginning of the period of adoption. PECO is currently assessing the impacts of this standard.

**2. Regulatory Matters**

The following matters below discuss the status of material regulatory and legislative proceedings of PECO.

**Distribution Base Rate Case Proceedings**

The following table shows the completed distribution rate case proceeding in 2018.

| | Filing Date | Requested Revenue Requirement Increase | Approved Revenue Requirement Increase | Approved ROE | Approval Date | Rate Effective Date |
|---|---|---|---|---|---|---|
| Electric | March 29, 2018 | \$82[(a)] | \$25[(a)] | N/A[(b)] | December 20, 2018 | January 1, 2019 |

(a) Includes the annual ongoing TCJA tax savings further discussed below.
(b) The PECO base rate case proceeding was resolved through a settlement agreement, which did not specify an approved ROE.

***Pending Transmission Formula Rate.*** On May 1, 2017, PECO filed a request with FERC seeking approval to update its transmission rates and change the manner in which PECO's transmission rate is determined from a fixed rate to a formula rate. The formula rate will be updated annually to ensure that under this rate customers pay the actual costs of providing transmission services. The formula rate filing includes a requested increase of \$22 million to PECO's annual transmission revenues and a requested rate of return on common equity of 11%, inclusive of a 50 basis point adder for being a member of a regional transmission organization. PECO requested that the new transmission rate be effective as of July 2017. On June 27, 2017, FERC issued an Order accepting the filing and suspending the proposed rates until December 1, 2017, subject to refund, and set the matter for hearing and settlement judge procedures. On May 4, 2018, the Chief Administrative Law Judge terminated settlement judge procedures and designated a new presiding judge. PECO cannot predict the outcome of this proceeding, or the transmission formula FERC may approve.

On May 11, 2018, pursuant to the transmission formula rate request discussed above, PECO made its first annual formula rate update, which included a revenue decrease of \$6 million. The revenue decrease of \$6 million included an approximately \$20 million reduction as a result of the tax savings associated with the TCJA. The updated transmission rate was effective June 1, 2018, subject to refund.

**Tax Cuts and Jobs Act**

**PECO Energy Company**
**Condensed Notes to Financial Statements**
**(Dollars in millions, unless otherwise noted)**

## 1. Significant Accounting Policies

### Description of Business

Incorporated in Pennsylvania in 1929, PECO Energy Company (PECO) is engaged principally in the purchase and regulated retail sale of electricity and the provision of transmission and distribution services to residential, commercial and industrial customers in southeastern Pennsylvania, including the City of Philadelphia, as well as the purchase and regulated retail sale of natural gas and the provision of distribution services to residential, commercial and industrial customers in the Pennsylvania counties surrounding the City of Philadelphia. PECO is subject to extensive regulation by the Pennsylvania Public Utility Commission (PAPUC) as to electric and gas distribution rates and service, the issuances of certain securities and certain other aspects of PECO's operations. PECO is a public utility under the Federal Power Act subject to regulation by the Federal Energy Regulatory Commission (FERC) as to transmission rates and certain other aspects of PECO's business and by the U.S. Department of Transportation as to pipeline safety and other aspects of gas operations. Additionally, PECO is also subject to the North American Electric Reliability Corporation (NERC) mandatory reliability standards. Pursuant to the Pennsylvania Electricity Generation Customer Choice and Competition Act of 1996 (Competition Act), the Commonwealth of Pennsylvania required the unbundling of retail electric services in Pennsylvania into separate energy transmission and distribution services with open retail competition for generation services. PECO serves as the local distribution company providing electric distribution services in its franchised service territory in southeastern Pennsylvania and energy service to customers who do not choose a competitive electric generation supplier or who choose to return to the utility after taking service from a competitive electric generation supplier.

### Basis of Presentation

PECO is a principal indirect subsidiary of Exelon Corporation (Exelon), which indirectly owns 100% of PECO's common stock. At December 31, 2019 and 2018, PECO's common stock without par value consisted of 500,000,000 shares authorized and 170,478,507 shares outstanding.

Accounting policies for regulated operations are in accordance with those prescribed by the regulatory authorities having jurisdiction, principally the PAPUC and FERC. The accompanying financial statements have been prepared in accordance with the accounting requirements of FERC as set forth in the Uniform System of Accounts (USOA) and accounting releases, which differ from accounting principles generally accepted in the United States of America (GAAP). The principal differences from GAAP include the exclusions of current maturities of long-term debt from current liabilities, the exclusion of debt issuance costs from long-term debt, the requirement to report deferred tax assets and liabilities separately rather than as a single amount, the classification of accrued taxes as assets and liabilities rather than a net amount, the exclusion of FIN 48 liabilities related to temporary income tax differences, the derecognition of operating leases from balance sheet, the classification of cloud computing costs, and the classification of certain other assets and liabilities as current instead of noncurrent.

PECO consolidates the accounts of entities in which PECO has a controlling financial interest, after the elimination of intercompany transactions. Where PECO does not have a controlling financial interest in an entity, proportionate consolidation, equity method accounting or accounting for investments in equity securities without readily determinable fair value is applied. PECO applies proportionate consolidation when they have an undivided interest in an asset and are proportionately liable for their share of each liability associated with the asset. PECO proportionately consolidates their undivided ownership interests in jointly owned electric plants and transmission facilities. Under proportionate consolidation, PECO separately records their proportionate share of the assets, liabilities, revenues and expenses related to the undivided interest in the asset. PECO applies equity method accounting when they have significant influence over an investee through an ownership in common stock, which generally approximates a 20% to 50% voting interest. PECO applies equity method accounting to certain investments and joint ventures, including certain financing trusts. Under equity method accounting, PECO reports their interest in the entity as an investment and PECO's percentage share of the earnings from the entity as single line items in their financial statements. PECO uses accounting for investments in equity securities without readily determinable fair values if they lack significant influence, which generally results when they hold less than 20% of the common stock of an entity. Under accounting for investments in equity securities without readily determinable fair values, PECO reports their investments at cost adjusted for changes from observable transactions for identical or similar investments of the same issuer, less impairment. Changes in measurement are reported in earnings.

PECO's investments in its subsidiaries, ExTel Corporation, LLC, PECO Wireless, LLC, PECO Energy Capital Trust IV (PECO Trust IV) and PECO Energy Capital Corporation (PECC) are accounted for under the equity method of accounting in accordance with the USOA. PECO Wireless, LLC is the parent company of ATNP Finance Company and sole member of PEC Financial Services, LLC. PECC is the general partner of PECO Energy Capital, L.P., which is the grantor of PECO Energy Capital Trust III (PECO Trust III). ExTel Corporation, LLC and PECO Wireless, LLC are consolidated in PECO's GAAP Financial Statements.

The accompanying financial statements as of December 31, 2019 and 2018 are audited, and in the opinion of the management of PECO, include all adjustments that are considered necessary for a fair presentation of PECO's financial statements in accordance with the Uniform System of Accounts (USOA). All adjustments are of a normal and recurring nature.

**Use of Estimates**

The preparation of financial statements of PECO in conformity with USOA and GAAP requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Areas in which significant estimates have been made include, but are not limited to, the accounting for nuclear decommissioning costs and other asset retirement obligations (AROs), pension and other postretirement benefits, the application of purchase accounting, inventory reserves, allowance for uncollectible accounts, goodwill and asset impairments, derivative instruments, unamortized energy contracts, fixed asset depreciation, environmental costs and other loss contingencies, taxes and unbilled energy revenues. Actual results could differ from those estimates.

**Accounting for the Effects of Regulation**

For their regulated electric and gas operations, PECO reflects the effects of cost-based rate regulation in their financial statements, which is required for entities with regulated operations that meet the following criteria: 1) rates are established or approved by a third-party regulator; (2) rates are designed to recover the entities' cost of providing services or products; and (3) there is a reasonable expectation that rates designed to recover costs can be charged to and collected from customers. PECO accounts for its regulated operations in accordance with regulatory and legislative guidance from the regulatory authorities having jurisdiction, principally the PAPUC, under state public utility laws and the FERC under various Federal laws. Regulatory assets and liabilities are amortized and the related expense or revenue is recognized in the Statements of Income consistent with the recovery or refund included in customer rates. PECO's regulatory assets and liabilities as of the balance sheet date are probable of being recovered or settled in future rates. If a separable portion of PECO's business was no longer able to meet the criteria discussed above, the affected entities would be required to eliminate from its financial statements the effects of regulation for that portion, which could have a material impact on their financial statements. See Note 2—Regulatory Matters for additional information.

PECO treats the impacts of a final rate order received after the balance sheet date but prior to the issuance of the financial statements as a non-recognized subsequent event, as the receipt of a final rate order is a separate and distinct event that has future impacts on the parties affected by the order.

**Revenues**

**Operating Revenues.** PECO's operating revenues generally consist of revenues from contracts with customers involving the sale and delivery of energy commodities and related products and services, utility revenues from alternative revenue programs (ARP), and realized and unrealized revenues recognized under mark-to-market energy commodity derivative contracts. PECO recognizes revenue from contracts with customers to depict the transfer of goods or services to customers in an amount that the entities expect to be entitled to in exchange for those goods or services. PECO's primary sources of revenue include regulated electric and natural gas tariff sales, distribution and transmission services. At the end of each month, PECO accrues an estimate for the unbilled amount of energy delivered or services provided to customers.

PECO records ARP revenue for its best estimate of the transmission revenue impacts resulting from future changes in rates that they believe are probable of approval by FERC in accordance with their formula rate mechanisms. See Note 2—Regulatory Matters for additional information.

**Option Contracts, Swaps and Commodity Derivatives**. Certain option contracts and swap arrangements that meet the definition of derivative instruments are recorded at fair value with subsequent changes in fair value recognized as revenue or expense. The classification of revenue or expense is based on the intent of the transaction. To the extent PECO receives full cost recovery for energy procurement and related costs from retail customers, it records the fair value of its energy swap contracts with unaffiliated suppliers as well as an offsetting regulatory asset or liability in its Balance Sheets. See Note 2—Regulatory Matters and Note 7—Derivative Financial Instruments for additional information.

**Taxes Directly Imposed on Revenue-Producing Transactions.** PECO collects certain taxes from customers such as sales and gross receipts taxes, along with other taxes, surcharges and fees, that are levied by state or local governments on the sale or distribution of gas and electricity. Some of these taxes are imposed on the customer, but paid by PECO, while others are imposed on PECO. Where these taxes are imposed on the customer, such as sales taxes, they are reported on a net basis with no impact to the Statements of Income. However, where these taxes are imposed on PECO, such as gross receipts taxes or other surcharges or fees, they are reported on a gross basis. Accordingly, revenues are recognized for the taxes collected from customers along with an offsetting expense. See Note 12 — Supplemental Financial Information for PECO's utility taxes that are presented on a gross basis.

**Income Taxes**

Deferred Federal and state income taxes are recorded on significant temporary differences between the book and tax basis of assets and liabilities and for tax benefits carried forward. Investment tax credits have been deferred in PECO's Balance Sheets and are recognized in book income over the life of the related property. PECO accounts for uncertain income tax positions using a benefit recognition model with a two-step approach; a more-likely-than-not recognition criterion; and a measurement approach that measures the position as the largest amount of tax benefit that is greater than 50% likely of being realized upon ultimate settlement. If it is not more-likely-than-not that the benefit of the tax position will be sustained on its technical merits, no benefit is recorded. Uncertain tax positions that relate only to timing of when an item is included on a tax return are considered to have met the recognition threshold. PECO recognizes accrued interest related to unrecognized tax benefits in Interest expense or Other income and deductions (interest income) and recognize penalties related to unrecognized tax benefits in Other, net in their Statements of Income.

**Cash and Cash Equivalents**

PECO considers investments purchased with an original maturity of three months or less to be cash equivalents.

**Restricted Cash and Investments**

Restricted cash and investments recorded in Account 134 represent restricted funds to satisfy designated current liabilities. As of December 31, 2019 and 2018, PECO's restricted cash primarily represented funds from the sales of assets that were subject to PECO's mortgage indenture.

Restricted cash and cash equivalents not available to satisfy current liabilities are classified as noncurrent assets.

**Allowance for Uncollectible Accounts**

The allowance for uncollectible accounts reflects PECO's best estimates of losses on the customers' accounts receivable balances. PECO estimates the allowance by applying loss rates developed specifically for each company to the outstanding receivable balance by customer risk segment. PECO's customer accounts are written off consistent with approved regulatory requirements.

**Inventories**

Inventory is recorded at the lower of weighted average cost or net realizable value. Provisions are recorded for excess and obsolete inventory. Fossil fuel, materials and supplies, and emissions allowances are generally included in inventory when purchased. Fossil fuel and emissions allowances are expensed to purchased power and fuel expense when used or sold. Materials and supplies generally includes transmission, distribution and generating plant materials and are expensed to operating and maintenance or capitalized to property, plant and equipment, as appropriate, when installed or used.

**Debt and Equity Security Investments**

***Equity Security Investments with Readily Determinable Fair Values.*** Equity securities held in the nuclear decommissioning trust (NDT), funds are classified as equity securities with readily determinable fair values. Realized and unrealized gains and losses, net of tax, on Generation's NDT funds associated with the Regulatory Agreement Units are included in regulatory liabilities at PECO and in Noncurrent payables to affiliates at Generation and in Miscellaneous deferred debits at PECO. See Note 2—Regulatory Matters for additional information regarding PECO's regulatory assets and liabilities and Note 5—Income Taxes and Note 4—Asset Retirement Obligations for additional information regarding marketable securities held by NDT funds.

**Property, Plant and Equipment**

Property, plant and equipment is recorded at original cost. Original cost includes construction-related direct labor and material costs. PECO also includes indirect construction costs including labor and related costs of departments associated with supporting construction activities. When appropriate, original cost also includes capitalized interest for Generation, Exelon Corporate and PHI and AFUDC for regulated property at PECO. The cost of repairs and maintenance, including planned major maintenance activities and minor replacements of property, is charged to Operating and maintenance expense as incurred.

Third parties reimburse PECO for all or a portion of expenditures for certain capital projects. Such contributions in aid of construction costs (CIAC) are recorded as a reduction to Property, plant and equipment, net. United States Department of Energy, (DOE), smart grid investment grant, (SGIG) and other funds reimbursed to PECO have been accounted for as CIAC.

Upon retirement, the cost of property, net of salvage, is charged to accumulated depreciation consistent with the composite and group methods of depreciation. Removal costs are capitalized to accumulated depreciation when incurred and recorded to depreciation expense over the life of the new asset constructed consistent with PECO's regulatory recovery method.

***Capitalized Software.*** Certain costs, such as design, coding, and testing incurred during the application development stage of software projects that are internally developed or purchased for operational use are capitalized within Property, plant and equipment. Such capitalized amounts are amortized ratably over the expected lives of the projects when they become operational, generally not to exceed five years. Certain other capitalized software costs are being amortized over longer lives based on the expected life or pursuant to prescribed regulatory requirements.

***Allowance for Funds Used During Construction (AFUDC).*** AFUDC is the cost, during the period of construction, of debt and equity funds used to finance construction projects for regulated operations. AFUDC is recorded to construction work in progress and as a non-cash credit to an allowance that is included in interest expense for debt-related funds and other income and deductions for equity-related funds. The rates used for capitalizing AFUDC are computed under a method prescribed by regulatory authorities.

See Note 3—Property, Plant and Equipment for additional information regarding property, plant and equipment.

**Depreciation and Amortization**

Depreciation is generally recorded over the estimated service lives of property, plant and equipment on a straight-line basis using the group, composite or unitary methods of depreciation. The group approach is typically for groups of similar assets that have approximately the same useful lives and the composite approach is used for dissimilar assets that have different lives. Under both methods, a reporting entity depreciates the assets over the average life of the assets in the group. PECO's depreciation expense includes the estimated cost of dismantling and removing plant from service upon retirement, which is consistent with each utility's regulatory recovery method. The estimated service lives for PECO is based on its most recent depreciation studies of historical asset retirement and removal cost experience. See Note 3—Property, Plant and Equipment for further information regarding depreciation.

Amortization of regulatory assets and liabilities are recorded over the recovery or refund period specified in the related legislation or regulatory order or agreement. When the recovery or refund period is less than one year, amortization is recorded to the line item in which the deferred cost or income would have originally been recorded in PECO's Statement of Income. Amortization of PECO's transmission formula rate regulatory assets are recorded to Operating revenues.

Amortization of income tax related regulatory assets and liabilities is generally recorded to Income tax expense. With the exception of income tax-related regulatory assets, when the recovery period is more than one year, the amortization is recorded to Depreciation and amortization (Account 403) in PECO's Statement of Income. For income tax related regulatory assets, amortization is generally recorded to Income tax expense (Account 409.1) in PECO's Statement of Income.

See Note 2—Regulatory Matters for additional information regarding PECO's regulatory assets.

**Asset Retirement Obligations**

AROs are accreted throughout each year to reflect the time value of money for these present value obligations through a charge to Operating and maintenance expense in the Statement of Income or, in the case of PECO's accretion, through an increase to regulatory assets. See Note 4—Asset Retirement Obligations for additional information.

**Guarantees**

PECO recognizes, at the inception of a guarantee, a liability for the fair market value of the obligations it has undertaken by issuing the guarantee, including the ongoing obligation to perform over the term of the guarantee in the event that the specified triggering events or conditions occur.

The liability that is initially recognized at the inception of the guarantee is reduced as PECO is released from risk under the guarantee. Depending on the nature of the guarantee, PECO's release from risk may be recognized only upon the expiration or settlement of the guarantee or by a systematic and rational amortization method over the term of the guarantee. See Note 10—Commitments and Contingencies for additional information.

**Asset Impairments**

***Long-Lived Assets.*** PECO regularly monitors and evaluates the carrying value of its long-lived assets and asset groups for recoverability whenever events or changes in circumstances indicate that the carrying value of those assets may not be recoverable. Indicators of impairment may include a deteriorating business climate, including, but not limited to, declines in energy prices, condition of the asset, specific regulatory disallowance, or plans to dispose of a long-lived asset significantly before the end of its useful life. PECO determines if long-lived assets and asset groups are impaired by comparing the undiscounted expected future cash flows to the carrying value. When the undiscounted cash flow analysis indicates a long-lived asset or asset group is not recoverable, the amount of the impairment loss is determined by measuring the excess of the carrying amount of the long-lived asset or asset group over its fair value.

**Derivative Financial Instruments**

PECO has entered into derivative natural gas contracts to hedge its long-term price risk in the natural gas market. PECO has entered into derivative contracts to procure electric supply through a competitive RFP process as outlined in its PAPUC-approved Default Service Provider Program (DSP Program). PECO does not enter into derivatives for proprietary trading purposes. PECO's derivative activities are in accordance with Exelon's Risk Management Policy.

All derivatives are recognized on the balance sheet at their fair value unless they qualify for certain exceptions, including the normal purchases and normal sales exception. Changes in fair value may be recorded as a regulatory asset or liability if there is an ability to recover or return the associated costs. Cash inflows and outflows related to derivative instruments are included as a component of operating, investing or financing cash flows in the Statement of Cash Flows, depending on the nature of each transaction.

Normal purchases and normal sales are contracts where physical delivery is probable, quantities are expected to be used or sold in the normal course of business over a reasonable period of time and will not be financially settled. Revenues and expenses on derivative contracts that qualify, and are designated, as normal purchases and normal sales are recognized when the underlying physical transaction is completed. While these contracts are considered derivative financial instruments, they are not required to be recorded at fair value, but rather are recorded on an accrual basis of accounting. See Note 7—Derivative Financial Instruments for additional information.

**Retirement Benefits**

PECO participates in Exelon's defined benefit pension plans and other postretirement plans. The measurement of the plan obligations and costs of providing benefits under these plans involve various factors, including numerous assumptions and inputs and accounting elections. The assumptions are reviewed annually and at any interim remeasurement of the plan obligations. The impact of assumption changes or experience different from that assumed on pension and other postretirement benefit obligations is recognized over time rather than immediately recognized in the Statement of Income. Gains or losses in excess of the greater of ten percent of the projected benefit obligation or the market related value (MRV) of plan assets are amortized over the expected average remaining service period of plan participants. See Note 6—Retirement Benefits for additional discussion of PECO's accounting for retirement benefits.

**New Accounting Standards**

**New Accounting Standards Adopted in 2019:** In 2019, PECO adopted the following new authoritative accounting guidance issued by the FASB.

*Cloud Computing Arrangements.* Aligns the requirements for capitalizing costs incurred to implement a cloud computing arrangement with the internal-use software guidance. As a result, certain implementation costs incurred in a cloud computing arrangement that are currently expensed as incurred will be deferred and amortized over the non-cancellable term of the arrangement plus any reasonably certain renewal periods. PECO early adopted this standard using a prospective approach. The guidance was not adopted for FERC reporting purposes and resulted in no change to the financial statements.

*Leases (Issued February 2016).* PECO applied the new guidance with the following transition practical expedients for GAAP reporting purposes:

a "package of three" expedients that must be taken together and allow entities to (1) not reassess whether existing contracts contain leases, (2) carry forward the existing lease classification, and (3) not reassess initial direct costs associated with existing leases,

an implementation expedient which allows the requirements of the standard in the period of adoption with no restatement of prior periods, and

a land easement expedient which allows entities to not evaluate land easements under the new standard at adoption if they were not previously accounted for as leases.

The guidance was not adopted for FERC reporting purposes and resulted in no change to the financial statements.

**New Accounting Standards Adopted as of January 1, 2020:** The following new authoritative accounting guidance issued by the FASB was adopted as of January 1, 2020 and will be reflected by PECO in its financial statements beginning in the first quarter of 2020.

*Impairment of Financial Instruments (Issued June 2016).* Provides for a new Current Expected Credit Loss (CECL) impairment model for specified financial instruments including loans, trade receivables, debt securities classified as held-to-maturity investments and net investments in leases recognized by a lessor. Under the new guidance, on initial recognition and at each reporting period, an entity is required to recognize an allowance that reflects its current estimate of credit losses expected to be incurred over the life of the financial instrument based on historical experience, current conditions and reasonable and supportable forecasts. The standard became effective January 1, 2020 and requires a modified retrospective transition approach through a cumulative-effect adjustment to retained earnings as of the beginning of the period of adoption. This standard is primarily applicable to PECO's trade accounts receivables balance. The guidance did not have a significant impact on the PECO's financial statements.

*Goodwill Impairment (Issued January 2017).* Simplifies the accounting for goodwill impairment by removing Step 2 of the current test, which requires calculation of a hypothetical purchase price allocation. Under the revised guidance, goodwill impairment will be measured as the amount by which a reporting unit's carrying value exceeds its fair value, not to exceed the carrying amount of goodwill (currently Step 1 of the two-step impairment test). Entities will continue to have the option to perform a qualitative assessment to determine if a quantitative impairment test is necessary. The standard was effective January 1, 2020 and must be applied on a prospective basis. PECO does not have goodwill as of December 31, 2019 and this updated guidance did not impact PECO's financial statements.

**2. Regulatory Matters**

The following matters below discuss the status of material regulatory and legislative proceedings of PECO.

**Utility Regulatory Matters**

**Distribution Base Rate Case Proceedings**

The following table shows the completed distribution rate case proceeding in 2019.

| | Filing Date | Requested Revenue Requirement Increase | Approved Revenue Requirement Increase | Approved ROE | Approval Date | Rate Effective Date |
|---|---|---|---|---|---|---|
| Electric | March 29, 2018 | $82 | 25 | N/A(a) | December 20, 2018 | January 1, 2019 |

(a) The PECO rate case proceeding was resolved through a settlement agreement, which did not specify an approved ROE.

**Transmission Formula Rates**

On May 1, 2017, PECO filed a request with FERC seeking approval to update its transmission rates and change the manner in which PECO's transmission rate is determined from a fixed rate to a formula rate. The formula rate will be updated annually to ensure that under this rate customers pay the actual costs of providing transmission services. The formula rate filing includes a requested increase of $22 million to PECO's annual transmission revenue requirement, which reflected a rate of return on common equity of 11%, inclusive of a 50 basis point adder for being a member of a regional transmission organization. On June 27, 2017, FERC issued an Order accepting the filing and suspending the proposed rates until December 1, 2017, subject to refund, and set the matter for hearing and settlement judge procedures.

On December 5, 2019, FERC issued an Order accepting without modification the settlement agreement filed by PECO and other parties in July 2019. The settlement results in an increase of approximately $14 million with a return on rate base of 7.62% compared to PECO's initial formula rate filing and allows for a rate of return on common equity of 10.35%, inclusive of a 50 basis point adder for being a member of the regional transmission organization. The settlement did not have a material impact on PECO's 2017, 2018, or 2019 annual transmission revenue requirements. PECO will update its rates in 2020 and refund estimated overcollections totaling approximately $28 million related to the amounts billed under the proposed rates in effect since 2017.

**PECO Energy Company**

Below is a list of PECO Energy Company's (PECO) internal audit reports issued from January 1, 2019 through December 31, 2020.

**PECO Internal Audit Reports Issued in 2019**

1. 2018 Enterprise-wide Metrics and Monitoring Review
2. 2019 BSC Cost Allocation Review
3. 2019 Exelon Utilities Meter to Cash Review
4. 2019 Political Action Committee Review

**PECO Internal Audit Reports Issued in 2020**

1. 2020 Accruals Review
2. 2020 BSC Cost Allocation Review
3. 2020 Exelon Real Estate and Facilities Operations
4. 2020 Exelon Utilities Energy Acquisition Operations Engagement
5. 2020 Exelon Utilities Field Operations
6. 2020 PECO Affiliated Interest Agreement Compliance Engagement
7. 2020 Significant Estimates Engagement
8. 2020 PECO DIMP Compliance Engagement (**performed under Attorney Client Privilege**)

## Management's Report on Internal Control Over Financial Reporting

The management of PECO Energy Company (PECO) is responsible for establishing and maintaining adequate internal control over financial reporting, as such term is defined in Exchange Act Rule 13a-15(f). Internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

PECO's management conducted an assessment of the effectiveness of PECO's internal control over financial reporting as of December 31, 2019. In making this assessment, management used the criteria in *Internal Control —Integrated Framework (2013)* issued by the Committee of Sponsoring Organizations of the Treadway Commission. Based on this assessment, PECO's management concluded that, as of December 31, 2019, PECO's internal control over financial reporting was effective.

February 11, 2020

## Report of Independent Registered Public Accounting Firm

To the Board of Directors and Shareholder of PECO Energy Company

***Opinion on the Financial Statements***

We have audited the consolidated financial statements, including the related notes, as listed in the index appearing under Item 15(a)(4)(i), and the financial statement schedule listed in the index appearing under Item 15(a)(4)(ii), of PECO Energy Company and its subsidiaries (the "Company") (collectively referred to as the "consolidated financial statements"). In our opinion, the consolidated financial statements present fairly, in all material respects, the financial position of the Company as of December 31, 2019 and 2018, and the results of its operations and its cash flows for each of the three years in the period ended December 31, 2019 in conformity with accounting principles generally accepted in the United States of America.

***Basis for Opinion***

These consolidated financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on the Company's consolidated financial statements based on our audits. We are a public accounting firm registered with the Public Company Accounting Oversight Board (United States) (PCAOB) and are required to be independent with respect to the Company in accordance with the U.S. federal securities laws and the applicable rules and regulations of the Securities and Exchange Commission and the PCAOB.

We conducted our audits of these consolidated financial statements in accordance with the standards of the PCAOB. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free of material misstatement, whether due to error or fraud. The Company is not required to have, nor were we engaged to perform, an audit of its internal control over financial reporting. As part of our audits we are required to obtain an understanding of internal control over financial reporting but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control over financial reporting. Accordingly, we express no such opinion.

Our audits included performing procedures to assess the risks of material misstatement of the consolidated financial statements, whether due to error or fraud, and performing procedures that respond to those risks. Such procedures included examining, on a test basis, evidence regarding the amounts and disclosures in the consolidated financial statements. Our audits also included evaluating the accounting principles used and significant estimates made by management, as well as evaluating the overall presentation of the consolidated financial statements. We believe that our audits provide a reasonable basis for our opinion.

/s/ PricewaterhouseCoopers LLP
Philadelphia, Pennsylvania
February 11, 2020

We have served as the Company's auditor since 1932.

## Management's Report on Internal Control Over Financial Reporting

The management of PECO Energy Company (PECO) is responsible for establishing and maintaining adequate internal control over financial reporting, as such term is defined in Exchange Act Rule 13a-15(f). Internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

PECO's management conducted an assessment of the effectiveness of PECO's internal control over financial reporting as of December 31, 2020. In making this assessment, management used the criteria in *Internal Control—Integrated Framework (2013)* issued by the Committee of Sponsoring Organizations of the Treadway Commission. Based on this assessment, PECO's management concluded that, as of December 31, 2020, PECO's internal control over financial reporting was effective.

February 24, 2021

## Report of Independent Registered Public Accounting Firm

To the Board of Directors and Shareholder of PECO Energy Company

### *Opinion on the Financial Statements*

We have audited the consolidated financial statements, including the related notes, as listed in the index appearing under Item 15(a)(4)(i), and the financial statement schedule listed in the index appearing under Item 15(a)(4)(ii), of PECO Energy Company and its subsidiaries (the "Company") (collectively referred to as the "consolidated financial statements"). In our opinion, the consolidated financial statements present fairly, in all material respects, the financial position of the Company as of December 31, 2020 and 2019, and the results of its operations and its cash flows for each of the three years in the period ended December 31, 2020 in conformity with accounting principles generally accepted in the United States of America.

### *Basis for Opinion*

These consolidated financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on the Company's consolidated financial statements based on our audits. We are a public accounting firm registered with the Public Company Accounting Oversight Board (United States) (PCAOB) and are required to be independent with respect to the Company in accordance with the U.S. federal securities laws and the applicable rules and regulations of the Securities and Exchange Commission and the PCAOB.

We conducted our audits of these consolidated financial statements in accordance with the standards of the PCAOB. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free of material misstatement, whether due to error or fraud. The Company is not required to have, nor were we engaged to perform, an audit of its internal control over financial reporting. As part of our audits we are required to obtain an understanding of internal control over financial reporting but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control over financial reporting. Accordingly, we express no such opinion.

Our audits included performing procedures to assess the risks of material misstatement of the consolidated financial statements, whether due to error or fraud, and performing procedures that respond to those risks. Such procedures included examining, on a test basis, evidence regarding the amounts and disclosures in the consolidated financial statements. Our audits also included evaluating the accounting principles used and significant estimates made by management, as well as evaluating the overall presentation of the consolidated financial statements. We believe that our audits provide a reasonable basis for our opinion.

### *Critical Audit Matters*

The critical audit matter communicated below is a matter arising from the current period audit of the consolidated financial statements that was communicated or required to be communicated to the audit committee and that (i) relates to accounts or disclosures that are material to the consolidated financial statements and (ii) involved our especially challenging, subjective, or complex judgments. The communication of critical audit matters does not alter in any way our opinion on the consolidated financial statements, taken as a whole, and we are not, by communicating the critical audit matter below, providing a separate opinion on the critical audit matter or on the accounts or disclosures to which it relates.

*Accounting for the Effects of Rate Regulation*

As described in Notes 1 and 3 to the consolidated financial statements, the Company applies the authoritative guidance for accounting for certain types of regulation, which requires management to record in their consolidated financial statements the effects of cost-based rate regulation for entities with regulated operations that meet the following criteria, (i) rates are established or approved by a third-party regulator; (ii) rates are designed to recover the entity's cost of providing services or products; and (iii) there is a reasonable expectation that rates designed to recover costs can be charged to and collected from customers. The Company accounts for its regulated operations in accordance with regulatory and legislative guidance from the regulatory authorities having jurisdiction under state public utility laws and the FERC under various Federal laws. Upon updates in material regulatory and legislative proceedings, where applicable, management will record new regulatory assets or liabilities and will assess whether it is probable that its currently recorded regulatory assets and liabilities will be recovered and settled, respectively, in future rates. As of December 31, 2020, there were approximately $801 million of regulatory assets and approximately $624 million of regulatory liabilities.

The principal considerations for our determination that performing procedures relating to management's accounting for the effects of rate regulation is a critical audit matter are the high degree of audit effort to assess the impact of regulation on accounting for regulatory assets and liabilities and to evaluate the complex audit evidence related to whether the regulatory assets and liabilities will be recovered and settled.

Addressing the matter involved performing procedures and evaluating audit evidence in connection with forming our overall opinion on the consolidated financial statements. These procedures included testing the effectiveness of controls relating to accounting for regulatory matters and evaluation of existing regulatory assets and liabilities. These procedures also included, among others, obtaining the Company's correspondence with regulators, evaluating the reasonableness of management's judgments regarding regulatory guidance and proceedings and the related accounting implications, and calculating regulatory assets and liabilities based on provisions outlined in rate orders and other correspondence with regulators.

/s/ PricewaterhouseCoopers LLP
Philadelphia, Pennsylvania
February 24, 2021

We have served as the Company's auditor since 1932.

Q. II-D-13

Regardless of whether a claim for negative or positive net salvage is made, attach an exhibit showing gross salvage, cost of removal, third party reimbursements, if any, and net salvage for the test year and 4 previous years.

A. II-D-13

Refer to Attachment II-D-13(a), which shows the 2017-2022 net salvage (cost of removal net of salvage value) that has been, or is expected to be, closed to the Accumulated Reserve. The 2021 and 2022 net salvage amounts are based on a three-year average of experienced net salvage for the years 2018-2020.

**PECO Energy Company**
**Net Salvage**
**2017-2022**

| | | | Year | | | | | |
|---|---|---|---|---|---|---|---|---|
| **Product Class** | **depr_group** | **Values** | **2017** | **2018** | **2019** | **2020** | **2021** | **2022** |
| **Common** | **PECO Common 3892 PA** | Sum of Cost of Removal | - | | | | - | - |
| | | Sum of Salvage | 442,515 | | | | - | - |
| | | Sum of Net Salvage | 442,515 | | | | - | - |
| | **PECO Common 3901 PA** | Sum of Cost of Removal | (61,869) | (929,522) | (896,456) | (7,073,267) | (2,966,415) | (2,966,415) |
| | | Sum of Salvage | - | - | - | - | - | - |
| | | Sum of Net Salvage | (61,869) | (929,522) | (896,456) | (7,073,267) | (2,966,415) | (2,966,415) |
| | **PECO Common 3902 PA** | Sum of Cost of Removal | (102,518) | (411,927) | (718,519) | (656,222) | (595,556) | (595,556) |
| | | Sum of Salvage | - | - | - | - | - | - |
| | | Sum of Net Salvage | (102,518) | (411,927) | (718,519) | (656,222) | (595,556) | (595,556) |
| | **PECO Common 3911 PA** | Sum of Cost of Removal | | | | (25,143) | (8,381) | (8,381) |
| | | Sum of Salvage | | | | - | - | - |
| | | Sum of Net Salvage | | | | (25,143) | (8,381) | (8,381) |
| | **PECO Common 3912 PA** | Sum of Cost of Removal | (5,543) | (642,517) | (669,743) | (2,595,699) | (1,302,653) | (1,302,653) |
| | | Sum of Salvage | - | - | - | - | - | - |
| | | Sum of Net Salvage | (5,543) | (642,517) | (669,743) | (2,595,699) | (1,302,653) | (1,302,653) |
| | **PECO Common 3913 PA** | Sum of Cost of Removal | | (18,296) | | | (6,099) | (6,099) |
| | | Sum of Salvage | | - | | | - | - |
| | | Sum of Net Salvage | | (18,296) | | | (6,099) | (6,099) |
| | **PECO Common 3921 PA** | Sum of Cost of Removal | - | | | (3) | (1) | (1) |
| | | Sum of Salvage | 6,850 | | | - | - | - |
| | | Sum of Net Salvage | 6,850 | | | (3) | (1) | (1) |
| | **PECO Common 3922 PA** | Sum of Cost of Removal | (5,104) | (5,670) | (3,690) | (3,063) | (4,141) | (4,141) |
| | | Sum of Salvage | 213,171 | 188,020 | 31,630 | 85,450 | 101,700 | 101,700 |
| | | Sum of Net Salvage | 208,066 | 182,350 | 27,940 | 82,388 | 97,559 | 97,559 |
| | **PECO Common 3923 PA** | Sum of Cost of Removal | (839) | (4,275) | (4,420) | (3,873) | (4,189) | (4,189) |
| | | Sum of Salvage | 306,350 | 415,280 | 103,220 | 220,750 | 246,417 | 246,417 |
| | | Sum of Net Salvage | 305,511 | 411,005 | 98,800 | 216,878 | 242,228 | 242,228 |
| | **PECO Common 3924 PA** | Sum of Cost of Removal | (15) | | | (3) | (1) | (1) |
| | | Sum of Salvage | 8,000 | | | - | - | - |
| | | Sum of Net Salvage | 7,985 | | | (3) | (1) | (1) |
| | **PECO Common 3925 PA** | Sum of Cost of Removal | (120) | (585) | (285) | (93) | (321) | (321) |
| | | Sum of Salvage | 24,700 | 12,075 | 6,030 | 4,710 | 7,605 | 7,605 |
| | | Sum of Net Salvage | 24,580 | 11,490 | 5,745 | 4,618 | 7,284 | 7,284 |
| | **PECO Common 3926 PA** | Sum of Cost of Removal | (45) | - | | (273) | (91) | (91) |
| | | Sum of Salvage | 2,000 | 250 | | - | 83 | 83 |
| | | Sum of Net Salvage | 1,955 | 250 | | (273) | (8) | (8) |
| | **PECO Common 3943 PA** | Sum of Cost of Removal | - | - | - | - | - | - |
| | | Sum of Salvage | 14,820 | 4,680 | 6,005 | 6,550 | 5,745 | 5,745 |
| | | Sum of Net Salvage | 14,820 | 4,680 | 6,005 | 6,550 | 5,745 | 5,745 |
| | **PECO Common 3970 PA** | Sum of Cost of Removal | | (4,292) | | | (1,431) | (1,431) |
| | | Sum of Salvage | | - | | | - | - |
| | | Sum of Net Salvage | | (4,292) | | | (1,431) | (1,431) |
| **Common Sum of Cost of Removal** | | | **(176,054)** | **(2,017,085)** | **(2,293,113)** | **(10,357,636)** | **(4,889,278)** | **(4,889,278)** |
| **Common Sum of Salvage** | | | **1,018,406** | **620,305** | **146,885** | **317,460** | **361,550** | **361,550** |
| **Common Sum of Net Salvage** | | | **842,352** | **(1,396,780)** | **(2,146,228)** | **(10,040,176)** | **(4,527,728)** | **(4,527,728)** |
| **Electric - Distribution Plant** | **PECO Elec 3640 PA LTIIP** | Sum of Cost of Removal | | (18,633) | | (162) | (6,265) | (6,265) |
| | | Sum of Salvage | | - | | - | - | - |
| | | Sum of Net Salvage | | (18,633) | | (162) | (6,265) | (6,265) |
| | **PECO Elec 3650 PA LTIIP** | Sum of Cost of Removal | (1,236) | (441) | | (2,761) | (1,067) | (1,067) |
| | | Sum of Salvage | - | 2,669 | | - | 890 | 890 |
| | | Sum of Net Salvage | (1,236) | 2,229 | | (2,761) | (177) | (177) |
| | **PECO Elec 3660 PA LTIIP** | Sum of Cost of Removal | (23,228) | | | (38,923) | (12,974) | (12,974) |
| | | Sum of Salvage | - | | | - | - | - |
| | | Sum of Net Salvage | (23,228) | | | (38,923) | (12,974) | (12,974) |
| | **PECO Elec 3670 PA LTIIP** | Sum of Cost of Removal | (11,123) | | | | - | - |
| | | Sum of Salvage | - | | | | - | - |
| | | Sum of Net Salvage | (11,123) | | | | - | - |
| | **PECO Elec 3707 SM RES PA** | Sum of Cost of Removal | | | | (19,479) | (6,493) | (6,493) |
| | | Sum of Salvage | | | | - | - | - |
| | | Sum of Net Salvage | | | | (19,479) | (6,493) | (6,493) |
| | **PECO Electric 3611 PA** | Sum of Cost of Removal | (177,838) | (91,681) | (100,120) | (296,648) | (162,816) | (162,816) |
| | | Sum of Salvage | - | - | 2,449 | 332,126 | 111,525 | 111,525 |
| | | Sum of Net Salvage | (177,838) | (91,681) | (97,671) | 35,479 | (51,291) | (51,291) |
| | **PECO Electric 3612 PA** | Sum of Cost of Removal | (14,574) | (553,533) | (219,973) | (1,915,465) | (896,324) | (896,324) |
| | | Sum of Salvage | - | 12,211 | 9,065 | 33,179 | 18,152 | 18,152 |
| | | Sum of Net Salvage | (14,574) | (541,322) | (210,909) | (1,882,286) | (878,172) | (878,172) |
| | **PECO Electric 3613 PA** | Sum of Cost of Removal | | (7,852) | (62,820) | (3,043) | (24,572) | (24,572) |
| | | Sum of Salvage | | - | 3,663 | - | 1,221 | 1,221 |
| | | Sum of Net Salvage | | (7,852) | (59,157) | (3,043) | (23,350) | (23,350) |
| | **PECO Electric 3620 PA** | Sum of Cost of Removal | (2,396,266) | (5,110,481) | (1,559,258) | (5,312,281) | (3,994,007) | (3,994,007) |
| | | Sum of Salvage | 71,684 | 3,179 | 55,653 | 103,428 | 54,087 | 54,087 |
| | | Sum of Net Salvage | (2,324,582) | (5,107,302) | (1,503,605) | (5,208,853) | (3,939,920) | (3,939,920) |
| | **PECO Electric 3640 PA** | Sum of Cost of Removal | (3,965,726) | (4,774,749) | (8,234,931) | (23,398,777) | (12,136,153) | (12,136,153) |
| | | Sum of Salvage | 629 | 528 | 370 | 2,824 | 1,241 | 1,241 |
| | | Sum of Net Salvage | (3,965,098) | (4,774,221) | (8,234,561) | (23,395,954) | (12,134,912) | (12,134,912) |
| | **PECO Electric 3650 PA** | Sum of Cost of Removal | (7,131,033) | (7,030,818) | (10,075,588) | (23,967,983) | (13,691,463) | (13,691,463) |
| | | Sum of Salvage | 36,918 | 655,744 | 413,035 | 186,449 | 418,409 | 418,409 |
| | | Sum of Net Salvage | (7,094,115) | (6,375,074) | (9,662,553) | (23,781,534) | (13,273,054) | (13,273,054) |
| | **PECO Electric 3660 PA** | Sum of Cost of Removal | (1,985,680) | (1,382,550) | (2,020,675) | (5,465,143) | (2,956,122) | (2,956,122) |
| | | Sum of Salvage | 326 | - | - | 17,223 | 5,741 | 5,741 |
| | | Sum of Net Salvage | (1,985,355) | (1,382,550) | (2,020,675) | (5,447,919) | (2,950,381) | (2,950,381) |
| | **PECO Electric 3670 PA** | Sum of Cost of Removal | (8,974,326) | (7,938,507) | (7,761,810) | (18,771,597) | (11,490,638) | (11,490,638) |
| | | Sum of Salvage | 37,532 | 657,526 | 412,291 | 191,582 | 420,466 | 420,466 |
| | | Sum of Net Salvage | (8,936,795) | (7,280,981) | (7,349,518) | (18,580,015) | (11,070,171) | (11,070,171) |
| | **PECO Electric 3680 PA** | Sum of Cost of Removal | (388,523) | (511,777) | (908,788) | (801,164) | (740,576) | (740,576) |
| | | Sum of Salvage | 2,701 | 24,620 | 400 | - | 8,340 | 8,340 |
| | | Sum of Net Salvage | (385,823) | (487,157) | (908,388) | (801,164) | (732,236) | (732,236) |
| | **PECO Electric 3691 PA** | Sum of Cost of Removal | (374,063) | (384,705) | (518,908) | (518,043) | (473,886) | (473,886) |
| | | Sum of Salvage | - | - | - | - | - | - |
| | | Sum of Net Salvage | (374,063) | (384,705) | (518,908) | (518,043) | (473,886) | (473,886) |
| | **PECO Electric 3692 PA** | Sum of Cost of Removal | (297,745) | (366,707) | (415,119) | (183,907) | (321,911) | (321,911) |
| | | Sum of Salvage | - | - | - | - | - | - |
| | | Sum of Net Salvage | (297,745) | (366,707) | (415,119) | (183,907) | (321,911) | (321,911) |
| | **PECO Electric 3730 PA** | Sum of Cost of Removal | (25,548) | (120,853) | (21,322) | (24,288) | (55,488) | (55,488) |
| | | Sum of Salvage | 292,227 | 17,191 | 12,510 | 21,391 | 17,031 | 17,031 |
| | | Sum of Net Salvage | 266,679 | (103,662) | (8,812) | (2,897) | (38,457) | (38,457) |
| | **PECO Electric 3731 PA** | Sum of Cost of Removal | (5,927) | (7,514) | (8,102) | (9,377) | (8,331) | (8,331) |
| | | Sum of Salvage | - | - | - | - | - | - |
| | | Sum of Net Salvage | (5,927) | (7,514) | (8,102) | (9,377) | (8,331) | (8,331) |
| | **PECO Electric 3732 PA** | Sum of Cost of Removal | (79,303) | (378,399) | (92,488) | (84,497) | (185,128) | (185,128) |
| | | Sum of Salvage | - | - | - | - | - | - |
| | | Sum of Net Salvage | (79,303) | (378,399) | (92,488) | (84,497) | (185,128) | (185,128) |
| **Electric - Distribution Plant Sum of Cost of Remova** | | | **(25,852,140)** | **(28,679,198)** | **(31,999,900)** | **(80,813,539)** | **(47,164,212)** | **(47,164,212)** |
| **Electric - Distribution Plant Sum of Salvage** | | | **442,015** | **1,373,668** | **909,436** | **888,202** | **1,057,102** | **1,057,102** |
| **Electric - Distribution Plant Sum of Net Salvage** | | | **(25,410,125)** | **(27,305,530)** | **(31,090,465)** | **(79,925,336)** | **(46,107,110)** | **(46,107,110)** |
| **Electric - General Plant** | **PECO Elec 3979 SM Comm E** | Sum of Cost of Removal | | (178,435) | (347,841) | (678,201) | (401,492) | (401,492) |
| | | Sum of Salvage | | 275,505 | - | - | 91,835 | 91,835 |
| | | Sum of Net Salvage | | 97,070 | (347,841) | (678,201) | (309,657) | (309,657) |
| | **PECO Electric 3901 PA** | Sum of Cost of Removal | | (204,708) | (228,173) | (262,520) | (231,800) | (231,800) |
| | | Sum of Salvage | | - | - | - | - | - |
| | | Sum of Net Salvage | | (204,708) | (228,173) | (262,520) | (231,800) | (231,800) |
| | **PECO Electric 3902 PA** | Sum of Cost of Removal | (10,073) | (79,493) | (187,566) | (63,269) | (110,110) | (110,110) |
| | | Sum of Salvage | - | - | - | - | - | - |
| | | Sum of Net Salvage | (10,073) | (79,493) | (187,566) | (63,269) | (110,110) | (110,110) |
| | **PECO Electric 3913 PA** | Sum of Cost of Removal | (19,611) | (99,533) | | | (33,178) | (33,178) |
| | | Sum of Salvage | - | - | | | - | - |
| | | Sum of Net Salvage | (19,611) | (99,533) | | | (33,178) | (33,178) |
| | **PECO Electric 3940 PA** | Sum of Cost of Removal | (9,547) | | (16,862) | (2,048) | (6,303) | (6,303) |
| | | Sum of Salvage | - | | - | - | - | - |
| | | Sum of Net Salvage | (9,547) | | (16,862) | (2,048) | (6,303) | (6,303) |
| | **PECO Electric 3970 PA** | Sum of Cost of Removal | (104,968) | (176,783) | (264,281) | (496,077) | (312,380) | (312,380) |
| | | Sum of Salvage | - | 255 | - | - | 85 | 85 |
| | | Sum of Net Salvage | (104,968) | (176,528) | (264,281) | (496,077) | (312,295) | (312,295) |
| | **PECO Electric 3980 PA** | Sum of Cost of Removal | | | | (6,036) | (2,012) | (2,012) |
| | | Sum of Salvage | | | | - | - | - |
| | | Sum of Net Salvage | | | | (6,036) | (2,012) | (2,012) |
| **Electric - General Plant Sum of Cost of Remova** | | | **(144,199)** | **(738,952)** | **(1,044,724)** | **(1,508,150)** | **(1,097,275)** | **(1,097,275)** |
| **Electric - General Plant Sum of Salvage** | | | **-** | **275,760** | **-** | **-** | **91,920** | **91,920** |
| **Electric - General Plant Sum of Net Salvage** | | | **(144,199)** | **(463,192)** | **(1,044,724)** | **(1,508,150)** | **(1,005,355)** | **(1,005,355)** |
| **Electric - Transmission Plant** | **PECO Electric 3501 PA** | Sum of Cost of Removal | | | | (22) | (7) | (7) |
| | | Sum of Salvage | | | | - | - | - |
| | | Sum of Net Salvage | | | | (22) | (7) | (7) |
| | **PECO Electric 3521 PA** | Sum of Cost of Removal | | (518,945) | | (421,034) | (313,326) | (313,326) |
| | | Sum of Salvage | | 511 | | 18,452 | 6,321 | 6,321 |
| | | Sum of Net Salvage | | (518,435) | | (402,582) | (307,006) | (307,006) |
| | **PECO Electric 3522 PA** | Sum of Cost of Removal | (464,127) | (117,687) | (6,081) | (198,117) | (107,295) | (107,295) |
| | | Sum of Salvage | 13,501 | 73 | - | 6,508 | 2,194 | 2,194 |
| | | Sum of Net Salvage | (450,626) | (117,614) | (6,081) | (191,608) | (105,101) | (105,101) |
| | **PECO Electric 3530 NJ** | Sum of Cost of Removal | | (88,749) | | | (29,583) | (29,583) |
| | | Sum of Salvage | | - | | | - | - |
| | | Sum of Net Salvage | | (88,749) | | | (29,583) | (29,583) |

| | | | | | | | | |
|---|---|---|---|---|---|---|---|---|
| | PECO Electric 3530 PA | Sum of Cost of Removal | (2,123,279) | (7,732,516) | (1,306,781) | (6,850,391) | (5,296,563) | (5,296,563) |
| | | Sum of Salvage | 129,096 | 76,239 | 176,002 | 133,670 | 128,637 | 128,637 |
| | | Sum of Net Salvage | (1,994,183) | (7,656,277) | (1,130,779) | (6,716,722) | (5,167,926) | (5,167,926) |
| | PECO Electric 3540 PA | Sum of Cost of Removal | (173,411) | (1,819,904) | (521,717) | (241,891) | (861,170) | (861,170) |
| | | Sum of Salvage | 39,069 | 16,208 | 18,039 | 1,476 | 11,908 | 11,908 |
| | | Sum of Net Salvage | (134,342) | (1,803,695) | (503,677) | (240,416) | (849,263) | (849,263) |
| | PECO Electric 3550 PA | Sum of Cost of Removal | | (60,835) | (411,583) | (318,050) | (263,489) | (263,489) |
| | | Sum of Salvage | | - | 12,699 | 1,892 | 4,863 | 4,863 |
| | | Sum of Net Salvage | | (60,835) | (398,884) | (316,158) | (258,626) | (258,626) |
| | PECO Electric 3560 PA | Sum of Cost of Removal | (178,960) | (2,130,850) | (183,542) | (314,108) | (876,167) | (876,167) |
| | | Sum of Salvage | 16,472 | 16,208 | 16,443 | 2,750 | 11,800 | 11,800 |
| | | Sum of Net Salvage | (162,488) | (2,114,641) | (167,099) | (311,359) | (864,367) | (864,367) |
| | PECO Electric 3570 PA | Sum of Cost of Removal | | (22,805) | | (92,602) | (38,469) | (38,469) |
| | | Sum of Salvage | | 19,260 | | - | 6,420 | 6,420 |
| | | Sum of Net Salvage | | (3,545) | | (92,602) | (32,049) | (32,049) |
| | PECO Electric 3580 PA | Sum of Cost of Removal | | (208,943) | (3,263) | (325,957) | (179,388) | (179,388) |
| | | Sum of Salvage | | 500,588 | - | 46,159 | 182,249 | 182,249 |
| | | Sum of Net Salvage | | 291,645 | (3,263) | (279,798) | 2,861 | 2,861 |
| **Electric - Transmission Plant Sum of Cost of Remova** | | | **(2,939,777)** | **(12,701,233)** | **(2,432,966)** | **(8,762,173)** | **(7,965,457)** | **(7,965,457)** |
| **Electric - Transmission Plant Sum of Salvage** | | | **198,139** | **629,088** | **223,182** | **210,906** | **354,392** | **354,392** |
| **Electric - Transmission Plant Sum of Net Salvage** | | | **(2,741,638)** | **(12,072,145)** | **(2,209,784)** | **(8,551,267)** | **(7,611,065)** | **(7,611,065)** |
| **Total Sum of Cost of Removal** | | | **(29,112,171)** | **(44,136,468)** | **(37,770,703)** | **(101,441,498)** | **(61,116,223)** | **(61,116,223)** |
| **Total Sum of Salvage** | | | **1,658,560** | **2,898,821** | **1,279,503** | **1,416,569** | **1,864,964** | **1,864,964** |
| **Total Sum of Net Salvage** | | | **(27,453,610)** | **(41,237,647)** | **(36,491,200)** | **(100,024,929)** | **(59,251,259)** | **(59,251,259)** |

Q. II-D-14 State the amount of debt interest utilized for test year income tax calculations, including the amount so utilized which has been allocated from the debt interest of an affiliate, and provide details of debt interest allocation computations.

A. II-D-14 Refer to Schedule D-18, page 96, line 7, of Exhibits MJT-1 and MJT-2 for the fully projected future test year and future test year, respectively, and PECO Statement No. 3, the direct testimony of Michael J. Trzaska. The Company has not included any debt interest of an affiliate in its interest synchronization calculation.

Q. II-D-15

Provide a schedule for the test year of Federal and Pennsylvania taxes other than income taxes, per books, pro forma at present rates, and pro forma at proposed rates, including the following tax categories:

a. Social security

b. Unemployment

c. Capital stock

d. Public utility

e. P.U.C. assessment

f. Other property taxes

g. Any other appropriate categories

A. II-D-15

Refer to the direct testimony of Michael J. Trzaska (PECO St. No. 3), Exhibit MJT-1, Schedule D-16, pages 81-83 for FPFTY budget amounts, pro forma at present rates and pro forma at proposed rates. Refer to Exhibit MJT-2, Schedule D-16, pages 81-83 for FTY budget amounts, pro forma at present rates and pro forma at proposed rates.

Q. II-D-16

Submit a schedule showing the adjustments from taxable net income per books to taxable net income pro forma under existing rates and pro forma under proposed rates, together with an explanation of all normalizing adjustments. Submit detailed calculations supporting taxable income before State and Federal income taxes where the income tax is subject to allocation due to operations in another state or due to operation of other taxable utility or non-utility business, or by operating divisions or areas.

A. II-D-16

Refer to Schedule D-18 of Exhibits MJT-1 and MJT-2 for the fully projected future test year and the future test year, respectively, and PECO Statement No. 3, the direct testimony of Michael J. Trzaska.

Q. II-D-17 Submit a schedule showing for the last 5 years the income tax refunds, plus interest – net of taxes, received from the Federal government due to prior years' claims.

A. II-D-17 Refer to Confidential Attachment II-D-17(a) for a schedule summarizing the Federal income tax refunds received by the Company in the last five years.

**THE ATTACHMENT IS CONFIDENTIAL AND IS SUBMITTED ONLY IN THE NON-PUBLIC VERSION OF THIS RESPONSE FILED WITH THE COMMISSION**

Q. II-D-18 Furnish a breakdown of major items comprising prepaid and deferred income tax charges and other deferred income tax credits, reserves and associated reversals on liberalized depreciation.

A. II-D-18 Refer to Attachment II-D-18(a).

**PECO Energy Company**
**Prepaid and Deferred Taxes**
**For the Period Ended December 31, 2020**
**(Thousand $)**

| | | Electric |
|---|---|---|
| **Accumulated Deferred Income Taxes (Account 190)** | | |
| | Accrued Benefits | 890 |
| | Asset Retirement Obligation | 4,656 |
| | Bad Debt | 27,641 |
| | Charitable Contributions | 400 |
| | Customer Advances For Construction | 708 |
| | Deferred Compensation Liability | 1,959 |
| | Deferred Rent | 225 |
| | Deferred Revenue | 402 |
| | FASB112 | 17 |
| | Incentive Pay | 11,970 |
| | Obsolete Inventory | 540 |
| | Other Current | 121 |
| | Other Equity Compensation | 936 |
| | Payroll Tax Deferral | 2,859 |
| | Pennsylvania NOL | 18,962 |
| | Post Retirement Benefits | 62,278 |
| | SA Unbilled Reserve | 1,007 |
| | Sales and Use Tax Payable | 1,194 |
| | Severance Payments | 183 |
| | Vacation Pay Change | 834 |
| | Vegetation Management Accrual | 6,484 |
| | Workers Compensation Reserve | 8,863 |
| | **Total Account 190** | 153,128 |
| **Accumulated Deferred Income Taxes(Accounts 282 &283)** | | |
| Other Property (Account 282) | | |
| | Liberalized Depreciation | (1,242,872) |
| | **Total Account 282** | (1,242,872) |
| Other (Account 283) | | |
| | AEC Receivable | (1,474) |
| | Amortization of Premium on Reacquired Debt | (222) |
| | Cloud Computing | (1,824) |
| | FAS 109 - Regulatory Asset | (164,894) |
| | Holiday Pay | (235) |
| | Other | (108) |
| | Pension | (85,684) |
| | Regulatory Assets | (26,122) |
| | State Tax Reserves | (3,147) |
| | **Total Account 283** | (283,712) |
| | **Total Accounts 282 and 283** | (1,526,583) |

Q. II-D-19 Explain how the Federal corporate graduated tax rates have been reflected for rate case purposes. If the Pennsylvania jurisdictional utility is part of a multi-corporate system, explain how the tax savings are allocated to each member of the system.

A. II-D-19 PECO joins with its parent Exelon Corporation ("Exelon") and other subsidiaries of Exelon in filing a consolidated federal income tax return. The Tax Cuts and Jobs Act, enacted on December 22, 2017, eliminated graduated corporate tax rates. Effective January 1, 2018, the Tax Cuts and Jobs Act established a flat 21% corporate tax rate. Therefore, there are no tax savings from graduated federal corporate income taxes to be reflected by PECO for rate making purposes.

Q. II-D-20 Explain the treatment given to costs of removal in the income tax calculation and the basis for such treatment.

A. II-D-20 The Company includes the cost of removal in the income tax calculation in accordance with Revenue Ruling 2000-7 of the Internal Revenue Service.  Costs of removal are treated as a deductible tax expense when incurred and need not be capitalized as part of the cost of the replacement asset under Section 263 or 263A of the Internal Revenue Code.

Q. II-D-21 Show income tax loss/gain carryovers from previous years. Show loss/gain carryovers by years of origin and amounts remaining by years at the beginning of the test year.

A. II-D-21 Tax loss carryovers are not currently included in rate base. Also, utilization of tax loss carryovers or generation of a tax loss within the test year, future test year, and fully projected future test year will not impact the calculation of tax expense.

Q. II-D-22

State whether the company eliminates tax savings by the payment of actual interest on construction work in progress not in rate base claim. If response is affirmative:

a. Set forth amount of construction claimed in this tax savings reduction and explain the basis for this amount.

b. Explain the manner in which the debt portion of this construction is determined for purposes of the deferral calculations.

c. State the interest rate used to calculate interest on this construction debt portion, and the manner in which it is derived.

d. Provide details of calculation to determine tax savings reduction, and state whether State taxes are increased to reflect the construction interest elimination.

A. II-D-22

The Company does not eliminate tax savings by the payment of actual interest on construction work in progress not in rate base claim.

Q. II-D-23

Under section 1552 of the Internal Revenue Code (26 U.S.C.A. § 1552) and 26 CFR 1.1552-1 (1983), if applicable, a parent company, in filing a consolidated income tax return for the group, must choose one of four options by which it must allocate total income tax liability of the group to the participating members to determine each member's tax liability to the Federal government (if this interrogatory is not applicable, so state):

a. State what option has been chosen by the group.

b. Provide, in summary form, the amount of tax liability that has been allocated to each of the participating members in the consolidated income tax return for the test year and the most recent 3 years for which data is available.

c. Provide a schedule, in summary form, of contributions, which were determined on the basis of separate tax return calculations, made by each of the participating members to the tax liability indicated in the consolidated group tax return. Provide total amounts of actual payments to the tax depository for the tax year, as computed on the basis of separate returns of members.

d. Provide the most recent annual income tax return for the group.

e. Provide details of the amount of the net operating losses of any member allocated to the income tax returns of each of the members of the consolidated group for the test year and the 3 most recent years for which data is available, together with a summary of the actual tax payments for those years.

f. Provide details of the amount of net negative income taxes, after all tax credits are accounted for, of any member allocated to the income tax return of each of the members of the consolidated group for the test year and the 3 most recent years for which data is available, together with a summary of the actual tax payments for those years.

A. II-D-23

a. PECO Energy Company is indirectly, wholly-owned by Exelon Corporation (Exelon). Internal Revenue Code Section 1552 provides for an allocation of consolidated income tax for "earnings and profits" purposes only. Exelon has elected option (a)(2), which in general, allocates consolidated tax (other than alternative minimum tax) among subsidiaries in accordance with Separate Return Tax. Generally, as set forth in the Exelon Tax Sharing Agreement, subsidiaries having positive allocations pay the amount of such allocations and subsidiaries having negative allocations receive payment for their allocation.

b. Refer to Confidential Attachments II-D-23(a), II-D-23(b), and II-D-23(c), which detail the tax liability allocated to each of the participating members in the consolidated federal income tax return for 2017, 2018, and 2019 respectively.

c. Exelon is the parent company of the Exelon consolidated group that includes PECO Energy Company and makes all necessary income tax payments to the Internal Revenue Service for the net tax liability that is due for the consolidated group. Exelon charges member companies that have positive federal income tax allocation and pays member companies that have a negative federal income tax allocation. The amounts Exelon receives from, or pays to, each member company are the same amounts as detailed in Confidential Attachments II-D-23(a), II-D-23(b), and II-D-23(c).

d. The most recent Federal income tax return filed by the consolidated group is for tax year 2019. The complete tax return contains over 1,000 pages. Confidential Attachment II-D-23(d) contains pages 1-6 of the Federal Form 1120 and a summary of taxable income by member company. Access to the complete Federal Income Tax return will be provided upon request.

e. The details of members with net operating losses are shown on Confidential Attachments II-D-23(a), II-D-23(b), and II-D-23(c) in the column entitled “Taxable Income”. Net operating losses are expressed as negative on the attachments. See part c of this response for details of tax payments.

f. The details of members with net negative income taxes are shown on Confidential Attachments II-D-23(a), II-D-23(b), and II-D-23(c) in the column entitled “Final Tax Sharing”. See part c of response for details of tax payments.

**THE ATTACHMENTS ARE CONFIDENTIAL AND ARE SUBMITTED ONLY IN THE NON-PUBLIC VERSION OF THIS RESPONSE FILED WITH THE COMMISSION.**

Q. II-D-24 Provide detailed computations by vintage year showing State and Federal deferred income taxes resulting from the use of accelerated tax depreciation associated with post-1969 public utility property, ADR rates, and accelerated tax depreciation associated with post-1980 public utility property under the Accelerated Cost Recovery System (ACRS).

A. II-D-24 The Company's tax records do not separately identify property installed prior to 1970 and property installed subsequent to 1969.

Q. II-D-25

Submit a schedule showing a breakdown of accumulated and unamortized investment tax credits, by vintage year and percentage rate, together with calculations supporting the amortized amount claimed as a reduction to pro forma income taxes.  Provide details of methods used to write-off the unamortized balances.

A. II-D-25

Prior years' deferred investment tax credits ("ITCs") are being recognized in income ratably over the remaining life used for depreciation for financial accounting purposes of the related property. Refer to Attachment II-D-25(a).

**PECO ENERGY COMPANY**
**YEAR OF REPORT: December 31, 2022**

| Line No. | Account Subdivisions (a) | Balance at Beginning of Year (b) | Deferred for Year: Account No. (c) | Deferred for Year: Amount (d) | Allocations to Current Year's Income: Account No. (e) | Allocations to Current Year's Income: Amount (f) | Adjustments (g) | Balance at End of Year (h) | Average Period of Allocation to Income (i) |
|---|---|---|---|---|---|---|---|---|---|
| 1 | Electric Utility | | | | | | | | |
| 2 | 6.5% | $ 353,914 | | $ - | 411.4 | $ 16,150 | $ - | $ 337,764 | 37 yrs |
| 3 | 10% | $ 10 | | $ - | 411.4 | $ - | $ - | $ 10 | 37 yrs |
| 4 | TOTAL Electric | $ 353,924 | | $ - | | $ 16,150 | $ - | $ 337,774 | |
| 5 | | | | | | A | | | |
| 6 | Common Utility | | | | | | | | |
| 7 | 4% | $ - | | $ - | 411.4 | $ - | $ - | $ - | 37 yrs |
| 8 | 10% | $ 6,814 | | $ - | 411.4 | $ 5,286 | $ - | $ 1,528 | 37 yrs |
| 9 | TOTAL COMMON | $ 6,814 | | $ - | | $ 5,286 | $ - | $ 1,528 | |
| 10 | | | | | | | | | |
| 11 | TOTAL ACCUM DEF'D ITC | $ 360,737 | | $ - | | $ 21,436 | $ - | $ 339,301 | |

| Allocation of Common Utility | Electric - D* | Electric - T* | Gas * | Total |
|---|---|---|---|---|
| Amortized 4% | $ - | $ - | $ - | $ - |
| Amortized 10% | $ 3,708 | $ 407 | $ 1,171 | $ 5,286 |
| TOTAL | $ 3,708 | $ 407 | $ 1,171 | $ 5,286 |
| | A | B | C | |

*Common allocated based on plant ratio 77.15% Electric Distribution, 7.69% Electric Transmission, and 22.16% Gas Distribution.

| Electric and Gas Total Activity | | |
|---|---|---|
| ITC - Electric (D) | ΣAs = | $ 19,858 |
| ITC - Electric (T) | ΣBs = | $ 407 |
| ITC - Gas | ΣCs = | $ 1,171 |
| | | $ 21,436 |

**PECO ENERGY COMPANY**
**YEAR OF REPORT: December 31, 2021**

| Line No. | Account Subdivisions | Balance at Beginning of Year | Deferred for Year: Account No. | Deferred for Year: Amount | Allocations to Current Year's Income: Account No. | Allocations to Current Year's Income: Amount | Adjustments | Balance at End of Year | Average Period of Allocation to Income |
|---|---|---|---|---|---|---|---|---|---|
| | (a) | (b) | (c) | (d) | (e) | (f) | (g) | (h) | (i) |
| 1 | Electric Utility | | | | | | | | |
| 2 | 6.5% | $ 370,063 | | $ - | 411.4 | $ 16,150 | $ - | $ 353,914 | 37 yrs |
| 3 | 10% | $ 10 | | $ - | 411.4 | $ - | $ - | $ 10 | 37 yrs |
| 4 | TOTAL Electric | $ 370,073 | | $ - | | $ 16,150 | $ - | $ 353,924 | |
| 5 | | | | | | A | | | |
| 6 | Common Utility | | | | | | | | |
| 7 | 4% | $ - | | $ - | 411.4 | $ - | $ - | $ - | 37 yrs |
| 8 | 10% | $ 15,461 | | $ - | 411.4 | $ 8,647 | $ - | $ 6,814 | 37 yrs |
| 9 | TOTAL COMMON | $ 15,461 | | $ - | | $ 8,647 | $ - | $ 6,814 | |
| 10 | | | | | | | | | |
| 11 | TOTAL ACCUM DEF'D ITC | $ 385,535 | | $ - | | $ 24,797 | $ - | $ 360,737 | |

| Allocation of Common Utility | Electric - D* | Electric - T* | Gas * | Total |
|---|---|---|---|---|
| Amortized 4% | $ - | $ - | $ - | $ - |
| Amortized 10% | $ 6,066 | $ 665 | $ 1,916 | $ 8,647 |
| TOTAL | $ 6,066 | $ 665 | $ 1,916 | $ 8,647 |
| | A | B | C | |

*Common allocated based on plant ratio 77.15% Electric Distribution, 7.69% Electric Transmission, and 22.16% Gas Distribution.

| Electric and Gas Total Activity | | |
|---|---|---|
| ITC - Electric (D) | ΣAs = | $ 22,216 |
| ITC - Electric (T) | ΣBs = | $ 665 |
| ITC - Gas | ΣCs = | $ 1,916 |
| | | $ 24,797 |

**PECO ENERGY COMPANY**
**YEAR OF REPORT: December 31, 2020**

| Line No. | Account Subdivisions (a) | Balance at Beginning of Year (b) | Deferred for Year: Account No. (c) | Deferred for Year: Amount (d) | Allocations to Current Year's Income: Account No. (e) | Allocations to Current Year's Income: Amount (f) | Adjustments (g) | Balance at End of Year (h) | Average Period of Allocation to Income (i) |
|---|---|---|---|---|---|---|---|---|---|
| 1 | Electric Utility | | | | | | | | |
| 2 | 6.5% | $ 386,214 | | $ - | 411.4 | $ 16,150 | $ - | $ 370,063 | 37 yrs |
| 3 | 10% | $ 10 | | $ - | 411.4 | $ - | $ - | $ 10 | 37 yrs |
| 4 | TOTAL Electric | $ 386,224 | | $ - | | $ 16,150 | $ - | $ 370,073 | |
| 5 | | | | | | A | | | |
| 6 | Common Utility | | | | | | | | |
| 7 | 4% | $ - | | $ - | 411.4 | $ - | $ - | $ - | 37 yrs |
| 8 | 10% | $ 25,466 | | $ - | 411.4 | $ 10,005 | $ - | $ 15,461 | 37 yrs |
| 9 | TOTAL COMMON | $ 25,466 | | $ - | | $ 10,005 | $ - | $ 15,461 | |
| 10 | | | | | | | | | |
| 11 | TOTAL ACCUM DEF'D ITC | $ 411,690 | | $ - | | $ 26,156 | $ - | $ 385,535 | |

| Allocation of Common Utility | Electric - D* | Electric - T* | Gas * | Total |
|---|---|---|---|---|
| Amortized 4% | $ - | $ - | $ - | $ - |
| Amortized 10% | $ 7,019 | $ 769 | $ 2,217 | $ 10,005 |
| TOTAL | $ 7,019 | $ 769 | $ 2,217 | $ 10,005 |
| | A | B | C | |

*Common allocated based on plant ratio 77.15% Electric Distribution, 7.69% Electric Transmission, and 22.16% Gas Distribution.

| Electric and Gas Total Activity | | |
|---|---|---|
| ITC - Electric (D) | ΣAs = | $ 23,169 |
| ITC - Electric (T) | ΣBs = | $ 769 |
| ITC - Gas | ΣCs = | $ 2,217 |
| | | $ 26,156 |

Q. II-D-26 Explain in detail by statement or exhibit the appropriateness of claiming any additional items, not otherwise specifically explained and supported in the statement of operating income.

A. II-D-26 Not applicable. The Company is not claiming any additional items not discussed, explained, and supported in the statements of operating income contained in Exhibits MJT-1 and MJT-2 and described in PECO Statement No. 3, the direct testimony of Michael J. Trzaska.

Q. II-D-27

If the utility’s operations include non-jurisdictional activities, provide a schedule which demonstrates the manner in which rate base and operating income date have been adjusted to develop the jurisdictional test year claim.

A. II-D-27

Refer to Exhibits MJT-1 and MJT-2 and PECO Statement No. 3, the direct testimony of Michael J. Trzaska. The manner in which non-jurisdictional amounts were calculated is discussed by Mr. Trzaska. For each claim that relates to operations that include non-jurisdictional activities, the calculation of the non-jurisdictional amount is shown in the applicable schedules of Exhibits MJT-1 and MJT-2 for the fully projected future test year and the future test year, respectively.